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February 11, 2005

BY OVERNIGHT DELIVERY

K. David Waddell, Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243

05-00048

Re: IDS Telcom Corp. and IDS Telcom, LLC

Dear Mr. Waddell:

IDS Telcom Corp. ("New IDS") and IDS Telcom, LLC ("Old IDS") (together, the "Applicants") hereby submit the attached Petition for approval of the proposed assignment of the Assets of Old IDS to New IDS and related transactions. A check in the amount of $25 is included to cover the required filing fee.

An original and thirteen (13) of copies of the attached filing are enclosed Please date stamp and return the extra copy of this letter in the enclosed self-addressed stamped envelope Please direct questions regarding this filing to the undersigned.

Respectfully submitted,

Catherine Wang
Edward S. Quill, Jr.

BEFORE THE
TENNESSEE REGULATORY AUTHORITY

In re: Joint Petition of **MCG CAPITAL CORPORATION,** **IDS TELCOM CORP.,** And **IDS TELCOM, LLC** For Authority to Complete an Assignment of Authority to Provide Competitive Services and Sale of Customer Base and Other Assets	Docket No. _______

JOINT PETITION

I. INTRODUCTION

MCG Capital Corporation ("Buyer" or "MCG"), IDS Telcom Corp ("New IDS") and IDS Telcom, LLC ("Old IDS")(together with Buyer and New IDS, "Applicants"), pursuant to Tenn Code Ann. § 65-4-112, respectfully request such authority as may be necessary or required from the Tennessee Regulatory Authority ("Authority") for New IDS (directly), and its ultimate indirect owner Buyer (through its wholly investment company, Cleartel Communications, Inc.), to acquire the assets of Old IDS identified in this Petition, including Old IDS's certifications, its customer base, and all other assets associated with its telecommunications services operations ("Assets") Petitioners request expedited consideration of this Joint Petition.

Old IDS and New IDS have entered into an Asset Purchase Agreement ("Agreement") whereby New IDS has agreed to purchase all of the Assets of Old IDS. As a result of the proposed transaction, Old IDS's Assets, including all of Old IDS's operations and customers, will be transferred and Old IDS's Tennessee certifications will be assigned to New IDS, a newly created, wholly owned direct subsidiary of Cleartel Following that transaction, Old IDS will cease to provide service in Tennessee and current Tennessee customers of Old IDS will be served by New IDS.

Petitioners emphasize that although as a technical matter the proposed transactions will result in a transfer of customers from Old IDS to New IDS, the transfer will be seamless and immediately following the proposed transactions, those customers will continue to receive service under the same rates, terms, and conditions of service as the services those customers currently receive. Moreover, because New IDS will continue to provide service under the "IDS" brand name, using the same IDS facilities and Assets, the transition will be virtually transparent to consumers of Old IDS's services in Tennessee in terms of the services that those consumers receive.

As set forth below, New IDS - through Buyer - has both significant financial resources and substantial experience in owning and operating regulated telecommunications services. As a result, the proposed transactions are structured to ensure that existing Old IDS customers will continue to enjoy uninterrupted service, while allowing the IDS operations to obtain needed financial resources. In light of the substantial benefits that the Petitioners expect from the proposed transactions, Petitioners seek expedited approval, to the extent necessary, to allow Petitioners to complete the proposed transactions as soon as possible

In support of this Petition, Petitioners provide the following information:

II. DESCRIPTION OF PETITIONERS

A. IDS Telcom, LLC

IDS Telcom, LLC ("Old IDS") is a leading integrated communications provider that operates within the southeastern U.S providing competitive telecommunications service mainly to residential and small to medium-sized business customers Old IDS offers a range of resold and facilities based telephone services, including voice and data private lines. Old IDS provides service over a state-of-the-art optical fiber network in Florida and via resold and unbundled network element arrangements with the ILEC elsewhere.

In addition to its operations in Tennessee, Old IDS is currently authorized by virtue of certification or other authorization to provide service throughout the BellSouth territory except in Louisiana. Old IDS is also authorized by the Federal Communications Commission ("FCC") to provide interstate and international services. In Tennessee, Old IDS is authorized to provide facilities-based and resold competitive telecommunications services pursuant to Certificates of Public Convenience and Necessity issued in Docket No. 00-01102. Further information concerning Old IDS and the services it provides have been previously submitted to the Authority, is publicly available, and is incorporated herein by reference.

B. MCG Capital Corporation/IDS Telcom Corp.

MCG Capital Corporation ("Buyer"), the ultimate owner (through its portfolio investment company, Cleartel Communications, Inc.) of IDS Telcom Corp. ("New IDS"), is a corporation formed under the laws of the State of Delaware with principal offices located at 1100 Wilson Boulevard, Suite 3000, Arlington, Virginia 22209 MCG is a solutions-focused publicly held financial services company (traded on the NASDAQ under the MCGC symbol) that provides financing and advisory services to a variety of small- and medium-sized companies throughout the United States with a focus on growth oriented companies.

MCG has ample managerial, technical, and financial qualifications to own and control New IDS and to oversee the operations currently conducted by Old IDS. In Tennessee, MCG currently holds an indirect controlling interest in NOW Communications, Inc ("NOW") through MCG's wholly owned portfolio investment company Cleartel Communications, Inc NOW is currently authorized to operate in Tennessee as a telecommunications carrier in Tennessee. NOW/Cleartel's management will likewise manage the day to day affairs of New IDS. In addition, MCG has previously held or currently holds interests in a number of telecommunications companies, including BridgeCom International, Inc., TruCom Corporation, Manhattan Telecommunications Corporation, Broadview Networks, Inc. and Broadview NP Acquisition Corp., and nii communications, Inc MCG's continuing involvement in overseeing the regulated ownership of these companies has provided MCG's management team with extensive telecommunications management experience.

Moreover, MCG has access to extensive financial resources. As of year end 2003, MCG had total assets of more than $791 million, including financial investments of more than $682 million, with total liabilities of approximately $367 million. MCG has positive shareholders' equity of approximately $464 million and had net income in 2003 of $41 9 million, including operating income of more than $71 7 million Recent financial information from MCG's recent SEC Form 10-Q is provided in Exhibit B. Additional information regarding MCG's financing and results of operations can be found in MCG's 2002 Annual Report available on line at. http://investor.mcgcapital.com/ and is incorporated herein by reference

III. CONTACTS

Questions or any correspondence, orders, or other materials pertaining to this Petition should be directed to the following.

For Buyer or New IDS:

Catherine Wang
Edward S. Quill, Jr.
Swidler Berlin LLP
3000 K Street NW
Suite 300
Washington, DC 20007
(202) 424-7500 (Tel)
(202) 424-7645 (Fax)
CWang@swidlaw com (E-Mail)
ESQuill@swidlaw com (E-Mail)

And:

Scott Kellogg
Associate General Counsel & Asst. Secretary
IDS Telcom Corp.
205 West Wacker Drive, Suite 2333
Chicago, IL 60606
(312) 658-1056 (Tel)
(312) 658-5487 (Fax)
skellogg@cleartel.com (E-Mail)

And:

Joseph Millstone
Chief Executive Officer
IDS Telcom, LLC
1525 NW 167th Street
Suite 200
Miami, FL 33169
(305) 612-4105 (Tel)
(305) 913-4011 (Fax)

IV. DESCRIPTION OF THE TRANSACTIONS

Petitioners propose to complete a series of transactions ("Transactions") through which New IDS, a wholly-owned direct subsidiary of Buyer's portfolio investment company Cleartel

Communications, Inc., will acquire all of the assets of Old IDS New IDS is a recently created Delaware corporation with headquarters located at 2855 S Congress Avenue, Delray Beach, Florida 33445.[1] New IDS and Old IDS have entered into an Asset Purchase Agreement ("Agreement") dated as of February 8, 2004. Pursuant to that Agreement, New IDS will acquire all of the operations, customers, and other Assets of Old IDS. As a result of the proposed Transactions, New IDS will replace Old IDS as the service provider operating in Tennessee. An illustrative chart of the proposed Transactions is provided in Exhibit C.

New IDS is well qualified to provide service in Tennessee. In connection with the proposed Transactions, New IDS will acquire all of the assets of Old IDS and will therefore own all of the assets and facilities currently used to provide service to customers in Tennessee New IDS's operations will be overseen by a well-qualified management team with substantial telecommunications experience and technical expertise New IDS will draw upon the expertise of the management team of its direct parent company, Cleartel Communications, Inc , which likewise manages the operations of Cleartel's other wholly owned Tennessee operating subsidiary, NOW New IDS will also rely on the managerial experience of Old IDS, which is also highly experienced and has substantial technical and managerial expertise New IDS will also have access to the highly qualified management team and substantial financial resources of MCG. Management biographies for New IDS's management team are provided in Exhibit A.

In order to allow New IDS to continue to provide service following the proposed Transactions, Petitioners respectfully request that the Authority allow Old IDS to transfer its existing Tennessee authorization to New IDS with the same conditions as previously granted to Old IDS. In the event that the Authority determines that the Tennessee authorization granted to

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1 Copies of the Articles of Incorporation of New IDS and a copy of New IDS's authority to conduct business in Tennessee are provided in Exhibit D

Old IDS cannot be transferred to New IDS, Petitioners respectfully request, in the alternative, that a second certification be granted to New IDS and that Old IDS's certification be cancelled effective as of the close of the proposed transaction

Although as a technical matter Old IDS customers will be transferred from Old IDS to New IDS in connection with the proposed Transactions, Petitioners emphasize that the migration of the IDS customers from Old IDS to New IDS will be transparent to the customers. Affected Old IDS customers will be notified in writing of the transfer of their service to New IDS and of their rights under federal law pursuant to the applicable rule of the FCC.[2] New IDS will acquire the "IDS" name and will continue to provide service under the "IDS" brand following the Transactions Furthermore, New IDS will adopt all of the tariffs (or make such other filings as may be necessary in compliance with the laws of Tennessee) and will continue to provide service under the same rates, terms and conditions as were previously provided by Old IDS As a result, the Transactions will be transparent to customers of Old IDS in terms of the services those customers receive.

V. PUBLIC INTEREST STATEMENT

The proposed Transactions described above will serve the public interest by ensuring that IDS customers enjoy continuity of high quality telecommunications service As demonstrated above and more fully in the Exhibits below, New IDS has the technical, managerial and financial resources required to ensure that New IDS can provide high quality services in Tennessee. New IDS is well-qualified to replace Old IDS as the service provider in Tennessee

The proposed Transaction will not cause customer confusion. Because there will be no change in the "IDS" brand name and the rates, terms and conditions of service will all continue

[2] 47 C F R. § 64 1120(e) A copy of the form of the customer notice letter which will be sent to such customers is provided in Exhibit E

without change, the proposed Transactions will be transparent to customers in Tennessee in terms of the services those customers receive. Indeed, New IDS will adopt the same tariffs currently on file for Old IDS. In sum, the proposed Transactions will enhance the ability of Petitioners to provide high-quality telecommunications services in Tennessee. This will invigorate competition and thereby benefit consumers of telecommunications services in Tennessee.

Given the increasingly complex and competitive nature of telecommunications markets and for other corporate reasons, Petitioners seek to complete the proposed Transactions as soon as possible. Accordingly, Petitioners respectfully request that the Authority process, consider and approve this Petition as expeditiously as possible.

VI. CONCLUSION

For the reasons stated above, Petitioners respectfully submit that the public interest, convenience, and necessity would be furthered by a grant of this Petition. Petitioners therefore respectfully request that the Authority consider and approve this Petition expeditiously to permit Petitioners to consummate the proposed Transactions as soon as possible

Respectfully submitted,

Catherine Wang
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Washington, DC 20007
(202) 424-7500 (Tel)
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ESQuill@swidlaw.com (E-Mail)

Counsel for Buyer and New IDS

Dated: February 11, 2005

List of Exhibit

EXHIBIT A

Management Information

Ken Baritz, CEO/President

Mr. Baritz has served as the CEO/President of IDS Telcom Corp.'s parent, Cleartel Communications, Inc., and its subsidiaries since August 2002. He served as President and Director of Talk America, Inc. from March 2000 to June 2001. Prior to joining Talk, Mr. Baritz served as Chairman and Chief Executive Officer of Access One from 1997 to 2000. Previous to Access One, he served as Chairman and Chief Executive Officer of AMNEX, Inc., a telecommunications company, and also was a Director of AMNEX from October 1992 through March 1997. Prior to his tenure at AMNEX, he served as a Vice President of Bear Stearns & Co., Inc., an investment-banking firm.

Jim Doherty, COO

Mr. Doherty has served as the COO of IDS Telcom Corp 's parent, Cleartel Communications, Inc , and its subsidiaries since August 2002. He previously served as Operations Manager for Talk America since 1999, where he was responsible for the day-to-day management of a 300 person customer care and provision facility. Prior to Talk/Access One, Mr. Doherty held the position of Director of Technical Operations with AMNEX from 1995 to 1999. Prior to that role, he served as Branch Operations Manager for National Telephone from 1986 to 1994. Mr. Doherty holds a degree in management

Terie Hannay, Sr. VP – Fiscal Operations

Ms. Hannay joined IDS Telecom Corp 's parent, Cleartel Communications, Inc. in October 2003 Her background includes serving as Michigan Regional Vice President, Customer Care for Charter Communications responsible for sales and customer support for 600,000-customer base While at Charter Communications, she consolidated 40 customer service sites into two sites running in a virtual environment as well as built a state of the art virtual call centers with over 400 employees. Prior to Charter Communications, Ms. Hannay served as Divisional Vice President Telecom Services at American Network Exchange (AMNEX) with responsibility for financial operations, call center operations, provisioning, customer care, MIS and Human Resources.

Don Zyck, CFO/VP-Finance

Mr. Zyck has served as the CFO/VP-Finance of IDS Telecom Corp 's parent, Cleartel Communications, Inc., and its subsidiaries since October 2002. Since 1985, he has been involved in the financial operations of public and private companies across numerous industries, including telecommunications, with responsibility for leading the functions of Accounting, Risk Management, Cash Management, Financial Planning and Analysis, Treasury, Bank Relations, Internal Audit and M&A. Most recently, Mr. Zyck served as the Senior Vice President and Acting CFO for Universal Access, Inc , a $120 million publicly traded telecommunications carrier. Previously, he served as Senior Vice President of Finance with Mesirow Financial and Treasurer and Controller with Cargill Investor Services, Inc. Mr. Zyck holds a BS in Finance.

Scott Kellogg, Associate General Counsel & Asst. Sec.

Mr Kellogg has ten years of experience in legal and governmental affairs. He joined IDS Telcom Corp.'s parent, Cleartel Communications, Inc., in December 2002 and has responsibility for regulatory affairs and corporate legal matters. He has served as counsel to competitive telecommunications carriers on a national basis since 1998. Outside of practicing law, Mr. Kellogg worked for three years in the Michigan House of Representatives and Senate.

EXHIBIT B

MCG Financial Information

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarter Ended September 30, 2004.

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-33377

MCG CAPITAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**54-1889518** (I.R.S. Employer Identification No.)
1100 Wilson Boulevard, Suite 3000 **Arlington, VA** (Address of principal executive office)	**22209** (Zip Code)

(703) 247-7500

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of shares of the registrant's Common Stock, $.01 par value, outstanding as of November 3, 2004 was 45,357,283.

MCG CAPITAL CORPORATION

FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2004

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PART I.FINANCIAL INFORMATION

In this Quarterly Report, the "Company", "MCG", "we", "us" and "our" refer to MCG Capital Corporation and its wholly owned consolidated subsidiaries and its affiliated securitization trusts unless the context otherwise requires

Selected Financial Data

The following table sets forth selected financial data from our unaudited financial statements. The selected financial data should be read in conjunction with our "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements (unaudited) and notes thereto included in this Quarterly Report.

(dollars in thousands except per share amounts and statistical data)	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Income statement data:				
Operating income	$ 24,837	$ 19,904	$ 69,826	$ 58,079
Net operating income before investment gains and losses	13,896	11,740	36,211	34,370
Net income	8,803	9,913	28,543	27,799
Per common share data:				
Earnings per common share basic and diluted	0.21	0.30	0.71	0.90
Net operating income before investment gains and losses per common share basic and diluted	0.33	0.36	0.90	1.11
Net asset value per common share (a)	12.18	11.99	12.18	11.99
Cash dividends declared per common share	0.42	0.42	1.26	1.23
Selected period-end balances:				
Total investment portfolio	$ 804,675	$ 611,927		
Total assets	1,049,588	801,354		
Borrowings	471,443	318,471		
Other data (at period-end):				
Number of portfolio companies	94	78		
Number of employees	102	54		

(a) Based on common shares outstanding at period-end.

Item 1.Financial Statements (unaudited)

MCG Capital Corporation

Consolidated Balance Sheets (unaudited)

(in thousands, except per share amounts)

		September30, 2004		December31, 2003
Assets				
Cash and cash equivalents	$	111,850	$	60,072
Cash, securitization accounts		109,852		33,434
Investments at fair value				
Commercial loans, (cost of $718,500 and $615,253, respectively)		709,041		605,551
Investments in equity securities, (cost of $ 128,955 and $112,850, respectively)		108,850		93,391
Unearned income on commercial loans		(13,216)		(16,416)
Total investments		804,675		682,526
Interest receivable		6,349		5,717
Other assets		16,862		9,166
Total assets	$	1,049,588	$	790,915
Liabilities				
Borrowings	$	471,443	$	304,131
Interest payable		634		1,185
Dividends payable		18,080		16,267
Other liabilities		7,149		5,382
Total liabilities		497,306		326,965
Commitments and contingencies				
Stockholders' Equity				
Preferred stock, par value $ 01, authorized 1 share, none issued and outstanding		—		—
Common stock, par value $ 01, authorized 100,000 shares, 45,356 issued and outstanding on September 30, 2004 and 38,732 issued and outstanding on December 31, 2003		454		387
Paid-in capital		641,157		529,168
Stockholder loans		(5,051)		(5,293)
Unearned compensation—restricted stock		(8,525)		(4,911)
Distributions in excess of earnings		(46,189)		(26,240)
Net unrealized depreciation on investments		(29,564)		(29,161)
Total stockholders' equity		552,282		463,950
Total liabilities and stockholders' equity	$	1,049,588	$	790,915

See notes to consolidated financial statements (unaudited).

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MCG Capital Corporation

Consolidated Statements of Operations (unaudited)

(in thousands, except per share amounts)

	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Operating income				
Interest and dividend income				
Non-affiliate investments (less than 5% owned)	$ **13,528**	$ 15,317	$ **38,704**	$ 48,719
Affiliate investments (5% to 25% owned)	**754**	1,341	**2,406**	3,426
Control investments (more than 25% owned)	**5,877**	1,008	**16,331**	2,105
Total interest and dividend income	**20,159**	17,666	**57,441**	54,250
Advisory fees and other income				
Non-affiliate investments (less than 5% owned) and other income	**2,319**	1,416	**6,427**	3,007
Affiliate investments (5% to 25% owned)	**495**	762	**495**	762
Control investments (more than 25% owned)	**1,864**	60	**5,463**	60
Total advisory fees and other income	**4,678**	2,238	**12,385**	3,829
Total operating income	**24,837**	19,904	**69,826**	58,079
Operating expenses				
Interest expense	**2,344**	2,701	**6,512**	7,429
Employee compensation:				
Salaries and benefits	3,469	1,759	9,697	5,800
Long-term incentive compensation	2,321	1,759	10,000	4,786
Total employee compensation	**5,790**	3,518	**19,697**	10,586
General and administrative expense	**2,807**	1,945	**7,406**	5,694
Total operating expenses	**10,941**	8,164	**33,615**	23,709
Net operating income before investment gains and losses	**13,896**	11,740	**36,211**	34,370
Net realized gains (losses) on investments				
Non-affiliate investments (less than 5% owned)	**936**	2,631	**2,924**	(7,511)
Affiliate investments (5% to 25% owned)	**(2,531)**	(48)	**(2,531)**	(48)
Control investments (more than 25% owned)	**—**	(519)	**(7,658)**	(11,916)
Total net realized gains (losses) on investments	**(1,595)**	2,064	**(7,265)**	(19,475)
Net change in unrealized appreciation (depreciation) on investments				
Non-affiliate investments (less than 5% owned)	**(2,274)**	222	**(2,399)**	18,957
Affiliate investments (5% to 25% owned)	**2,182**	(803)	**(1,185)**	941
Control investments (more than 25% owned)	**(3,406)**	(3,310)	**3,181**	(6,994)
Total net change in unrealized appreciation (depreciation) on investments	**(3,498)**	(3,891)	**(403)**	12,904
Net investment losses	**(5,093)**	(1,827)	**(7,668)**	(6,571)

Net income	**$**	**8,803**	$	9,913	**$**	**28,543**	$	27,799
Earnings per common share basic and diluted	**$**	**0.21**	$	0.30	**$**	**0.71**	$	0.90
Cash dividends declared per common share	**$**	**0.42**	$	0.42	**$**	**1.26**	$	1.23
Weighted average common shares outstanding		**42,646**		32,878		**40,049**		31,033
Weighted average common shares outstanding and dilutive common stock equivalents		**42,676**		32,906		**40,104**		31,042

See notes to consolidated financial statements (unaudited).

MCG Capital Corporation

Consolidated Statements of Stockholders' Equity (unaudited)

(in thousands, except per share amounts)

	Common stock		Paid-in Capital	Stock-holder Loans	Unearned Compen-sation—Restrictedstock	Distributions (in excess of) less than Earnings	NetUnrealized Depreciationon Investments	Total Stockholders' Equity
	Shares	Amount						
Balance December 31, 2002	31,259	$ 313	$ 419,961	$ (5,513)	$ (8,566)	$ (1,824)	$ (43,121)	$ 361,250
Net income						14,895	12,904	27,799
Issuance of common shares, net of costs	7,475	74	108,759					108,833
Dividends declared, $1.23 per share						(36,747)		(36,747)
Dividend reinvestment	2	—	38					38
Amortization of restricted stock awards					3,094			3,094
Change in vesting of restricted stock awards			506		(506)			—
Reduction in employee loans	(7)		(135)	218	89			172
Balance September 30, 2003	38,729	$ 387	$ 529,129	$ (5,295)	$ (5,889)	$ (23,676)	$ (30,217)	$ 464,439
Balance December 31, 2003	38,732	$ 387	$ 529,168	$ (5,293)	$ (4,911)	$ (26,240)	$ (29,161)	$ 463,950
Net income (loss)						28,946	(403)	28,543
Issuance of common shares, net of costs	6,622	67	100,048					100,115
Dividends declared, $1.26 per share						(48,895)		(48,895)
Dividend reinvestment	2	—	72					72
Amortization of restricted stock awards					8,279			8,279
Change in vesting of restricted stock awards			11,903		(11,903)			—
Reduction in employee loans			(34)	242	10			218
Balance September 30, 2004	45,356	$ 454	$ 641,157	$ (5,051)	$ (8,525)	$ (46,189)	$ (29,564)	$ 552,282

See notes to consolidated financial statements (unaudited).

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MCG Capital Corporation

Consolidated Statements of Cash Flows (unaudited)

(in thousands)

	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Operating activities		
Net income	$ 28,543	$ 27,799
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	765	429
Amortization of restricted stock awards	8,279	3,094
Amortization of deferred debt issuance costs	995	968
Net realized (gains) losses on investments	7,265	19,475
Net change in unrealized depreciation (appreciation) on investments	403	(12,904)
Increase in cash—securitization accounts from interest collections	3,170	2,403
Increase in interest receivable	(1,069)	(414)
(Increase) decrease in accrued payment-in-kind interest and dividends	548	(9,676)
Decrease in unearned income	(5,520)	(3,231)
(Increase) decrease in other assets	(2,750)	1,275
Decrease in interest payable	(551)	(341)
Increase (decrease) in other liabilities	3,489	579
Net cash provided by operating activities	43,567	29,456
Investing activities		
Originations, draws and advances on loans	(267,756)	(34,340)
Principal payments on loans	144,096	105,693
Purchase of equity investments	(14,791)	(4,980)
Proceeds from sales of equity investments	13,746	5,570
Purchase of premises, equipment and software	(401)	(1,105)
Net cash provided by (used in) investing activities	(125,106)	70,838
Financing activities		
Net increase (payments) on borrowings	165,528	(44,752)
Decrease in cash—securitization accounts for paydown of principal on debt	21,133	19,060
Increase in cash—securitization accounts for future loan acquisitions	(98,936)	—
Payment of financing costs	(6,010)	(2)
Dividends paid	(48,803)	(38,446)
Issuance of common stock, net of costs	100,187	108,871
Repayment of loans to officers/shareholders	218	177
Net cash used in financing activities	133,317	44,908
Increase in cash and cash equivalents	51,778	145,202
Cash and cash equivalents at beginning of period	60,072	9,389
Cash and cash equivalents at end of period	$ 111,850	$ 154,591

See notes to consolidated financial statements (unaudited).

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MCG Capital Corporation

Consolidated Schedule of Investments (unaudited)

September 30, 2004

(dollars in thousands)

Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost	September 30, 2004 Fair Value
Non-affiliate investments (less than 5% owned):					
Allen's T.V. Cable Service, Inc.	Cable	Senior Debt		$ 7,130	$ 7,130
		Subordinated Debt		1,000	1,000
Ames True Temper, Inc.	Industrial Equipment	Senior Debt		997	1,011
Auto Europe, LLC	Equipment Leasing	Senior Debt		7,553	7,553
Badoud Enterprises, Inc (2)	Newspaper	Senior Debt		6,100	6,100
Boucher Communications, Inc. (2)	Publishing	Senior Debt		1,100	1,100
		Stock Appreciation Rights		—	387
Builders FirstSource, Inc.	Building & Development	Senior Debt		4,975	5,012
		Subordinated Debt		2,000	2,020
Cambridge Information Group, Inc. (2)	Information Services	Senior Debt		15,425	15,425
CCG Consulting, Inc.	Business Services	Senior Debt		1,424	1,424
		Warrants to purchase Common Stock	19.9 %	—	—
Communications & Power Industries, Inc.	Aerospace & Defense	Senior Debt		1,990	2,021
Community Media Group Inc. (2)	Newspaper	Senior Debt		24,673	24,673
Creative Loafing, Inc. (2)	Newspaper	Senior Debt		19,900	19,900
Crescent Publishing Company, LLC (2)	Newspaper	Senior Debt		10,382	10,382
Cruz Bay Publishing, Inc. (2)	Publishing	Senior Debt		6,342	6,342
		Subordinated Debt		10,383	10,383
dick clark productions, inc.	Broadcasting	Subordinated Debt		17,531	17,531
		Warrants to purchase Common Stock	5.3 %	858	859
		Common Stock	0.5 %	210	131

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost	September 30, 2004 Fair Value
DowdenHealthMedia,Inc.	Publishing	Senior Debt		$ 500	$ 500
The e-Media Club I, LLC (6)	Investment Fund	LLC Interest	0 8 %	88	37
Financial Technologies International, Inc. (2)	Technology	Senior Debt	4.2 %	18,000	17,000
		Warrants to purchase Common Stock		—	—
GCA Services Group, Inc.	Commercial Services	Subordinated Debt		10,000	10,000
Graycom, L.C. (6)	Telecommunications	Warrants to purchase membership interest in LLC	27 8 %	71	53
The Hillman Group, Inc.	Industrial Equipment	Senior Debt		5,970	6,037
Home Interiors & Gifts, Inc	Home Furnishings	Senior Debt		4,922	4,703
Home Town Telephone, LLC(6)	Telecommunications	Warrants to purchase membership interest in LLC	27.8 %	—	—
I-55 Internet Services, Inc.	Telecommunications	Senior Debt		2,163	2,163
		Warrants to purchase Common Stock	20 0 %	366	403
IDS Telcom LLC	Telecommunications	Senior Debt		18,823	18,823
		Warrants to purchase membership interest in LLC	27 8 %	2,693	2,965
Images.com, Inc.	Information Services	Senior Debt		3,158	3,158
Information Today, Inc. (2)	Information Services	Senior Debt		8,792	8,792
International Media Group, Inc.	Broadcasting	Senior Debt		8,000	8,000
Jeffrey A Stern (6)	Other	Senior Debt		45	45
Jenzabar, Inc. (2)	Technology	Senior Debt		12,000	12,000
		Subordinated Debt		7,099	7,099
		Senior Preferred Stock	100.0 %	5,141	5,141
		Subordinated Preferred Stock	100 0 %	1,106	1,106
		Warrants to purchase Common Stock	18.0 %	422	607

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost	Fair Value
The Joseph F. Biddle Publishing Company (2)	Newspaper	Senior Debt		$ 9,105	$ 9,105
Joseph C. Millstone	Telecommunications	Senior Debt		500	500
Knowledge Learning Corporation	Healthcare	Senior Debt		7,138	7,183
The Korea Times Los Angeles, Inc.	Newspaper	Senior Debt		9,914	9,914
La Grange Acquisition, L.P.	Oil and Gas	Senior Debt		5,000	5,047
Lakeland Finance, LLC	Leisure	Senior Debt		5,749	5,749
		Subordinated Debt		1,500	1,500
Le-Nature's, Inc.	Beverage and Tobacco	Senior Debt		2,992	3,032
Maidenform, Inc.	Clothing/Textiles	Senior Debt		4,944	5,030
		Subordinated Debt		1,808	1,844
Majesco Holdings Inc.(6)(15)	Leisure	Common Stock	0.3%	57	50
Managed Health Care Associates	Drugs	Senior Debt		6,194	6,194
Metropolitan Telecommunications Holding Company (2)	Telecommunications	Senior Debt		13,925	13,925
		Subordinated Debt		12,328	12,328
		Preferred Stock	100.0%	1,964	1,962
		Warrants to purchase Common Stock	28.0%	2,805	4,695
McGinnis-Johnson Consulting, LLC (2)	Newspaper	Unsecured Note		1,000	1,000
MedAssets, Inc.	Healthcare	Senior Debt		4,517	4,574
		Subordinated Debt		2,500	2,550
The Meow Mix Company	Food Products	Senior Debt		3,760	3,699
Miles Media Holding, Inc. (2)	Publishing	Senior Debt		7,743	7,743
		Warrants to purchase Common Stock	12.1%	20	217
Minnesota Publishers, Inc. (2)	Newspaper	Senior Debt		14,250	14,250
MultiPlan, Inc.	Insurance	Senior Debt		4,975	5,025
Nalco Company	Ecological Services	Senior Debt		4,220	4,275
New Century Companies, Inc. (6)	Industrial Equipment	Common Stock	2.3%	157	48
		Warrants to purchase Common Stock	0.4%	—	—

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New Vision Broadcasting, LLC (2)	Broadcasting	Senior Debt		$ 16,033	$ 16,033
NewWave Communications, LLC (2)	Cable	Senior Debt		11,348	11,348
nii communications, inc. (2)	Telecommunications	Senior Debt		7,642	7,642
		Common Stock	2.8 %	400	189
		Warrants to purchase Common Stock	36.5 %	1,218	2,074
PartMiner, Inc. (2)	Information Services	Senior Debt		6,009	6,009
Powercom Corporation (2)	Telecommunications	Senior Debt		2,081	2,081
		Warrants to purchase Class A Common Stock	20.7 %	278	103
R.R. Bowker LLC (2)	Information Services	Senior Debt		17,450	17,450
Refco Group	Finance	Senior Debt		5,000	4,998
Sheridan Healthcare, Inc.	Healthcare	Senior Debt		2,925	2,962
Solo Cup Company	Containers & Glass	Senior Debt		4,979	5,026
Sterigenics International, Inc.	Healthcare	Senior Debt		4,988	5,050
Stonebridge Press, Inc. (2)	Newspaper	Senior Debt		5,204	5,204
SXC Health Solutions, Inc. (2) (13)	Technology	Senior Debt		7,600	7,600
Talk America Holdings,	Telecommunications	Common Stock	0.8 %	499	1,089
Inc. (6)		Warrants to purchase Common Stock	0.7 %	25	150
Tippmann Sports, LLC	Leisure Goods	Senior Debt		8,362	8,362
Tower Resource Management, Inc. (6)	Telecommunications	Warrants to purchase Common Stock	8.9 %	—	—
United Industries Corporation	Farming & Agriculture	Senior Debt		2,989	3,032
U. S. I. Holdings Corporation	Insurance	Senior Debt		997	1,009
VS&A-PBI Holding LLC(6)	Publishing	LLC Interest	0.8 %	500	—

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Waddington North America, Inc.	Containers & Glass	Senior Debt		$ 4,900	$ 4,883
Wicks Business Information, LLC	Publishing	Unsecured Note		200	200
Wiesner Publishing Company, LLC (2)	Publishing	Senior Debt		6,763	6,763
		Subordinated Debt		4,105	4,105
		Warrants to purchase membership interest in LLC	15.0 %	406	211
WirelessLines II, Inc.	Telecommunications	Senior Debt		351	351
Witter Publishing Co , Inc.	Publishing	Senior Debt		2,601	2,000
		Warrants to purchase Common Stock	20.0 %	146	—
Wyoming Newspapers, Inc. (2)	Newspapers	Senior Debt		15,000	15,000
Total Non-affiliate investments				519,396	521,379
Affiliate investments(3):					
All Island Media, Inc.	Newspaper	Senior Debt		6,800	6,800
		Common Stock	8.9 %	500	500
Country Media, Inc.	Newspaper	Senior Debt		6,807	6,807
		Common Stock	6.3 %	100	153
Executive Enterprise Institute LLC (6)	Business Services	LLC Interest	10.0 %	301	—

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost	September 30, 2004 Fair Value
On Target Media, LLC	Advertising	Senior Debt		$ 20,000	$ 20,000
		Subordinated Debt		10,000	10,000
		Class A LLC Interest	6.8 %	1,470	1,470
		Class B LLC Interest	16.9 %	—	—
Sunshine Media Delaware, LLC (2)	Publishing	Senior Debt		12,683	8,741
		Class A LLC Interest	12.8 %	564	—
		Warrants to purchase Class B LLC interest	100.0 %	—	—
ViewTrust Technology, Inc. (6)	Technology	Common Stock	7.5 %	1	3
Total Affiliate investments				**59,226**	**54,474**
Control investments: Non-majority-owned (4):					
Creatas, L.L.C. (2)	Information Services	Senior Debt		18,212	18,212
		Investor Class LLC Interest	100.0 %	1,273	14,952
ETC Group, LLC (10)	Publishing	Guaranty ($501)			
		Senior Debt		1,200	1,166
		Series A LLC Interest	100.0 %	650	—
		Series C LLC Interest	100.0 %	100	—
Fawcette Technical Publications Holding (2)	Publishing	Senior Debt		12,440	12,440
		Subordinated Debt		3,940	3,940
		Series A Preferred Stock	100.0 %	2,569	1,743
		Common Stock	36.0 %	—	—
National Systems Integration, Inc. (6) (9)	Security Alarm	Senior Debt		910	—
		Class B-2 Preferred Stock	100.0 %	4,409	—
		Common Stock	46.0 %	—	—
Platinum Wireless, Inc.	Telecommunications	Senior Debt		836	836
		Common Stock	37.0 %	4,640	4,534
		Option to purchase Common Stock	1.5 %	272	99
Total Control investments: Non-majority-owned				**51,451**	**57,922**

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost	September 30, 2004 Fair Value
Control investments: Majority-owned (5):					
Bridgecom Holdings, Inc. (2) (11)	Telecommunications	Senior Debt		$ 23,634	$ 23,634
		Preferred Stock	100.0%	39,717	39,717
		Common Stock	100.0%	—	662
ClearTel Communications, Inc. (2) (14)	Telecommunications	Senior Debt		23,048	23,048
		Subordinated Debt		2,363	2,363
		Preferred Stock	100.0%	9,195	663
		Common Stock	100.0%	540	—
		Guaranty ($196)			
Copperstate Technologies, Inc.	Security Alarm	Senior Debt		1,060	1,060
		Class A Common Stock	93.0%	2,000	1,212
		Class B Common Stock		—	—
		Warrants to purchase Class B Common Stock	97.3%	—	—
		Guaranty ($1,000)			
Corporate Legal Times L.L.C.	Publishing	Senior Debt		4,625	4,556
		Subordinated Debt		1,338	—
		LLC Interest	90.6%	313	—
Crystal Media Network, LLC (6)(7)	Broadcasting	Senior Debt		932	932
		LLC Interest	100.0%	6,132	4,802
Interactive Business Solutions, Inc.	Security Alarm	Senior Debt		75	75
		Common Stock	100.0%	2,750	574
Midwest Tower Partners, LLC (2)	Telecommunications	Subordinated Debt		15,980	15,980
		Preferred Stock	91.0%	1,770	1,770
		LLC Interest	79.2%	201	169
Superior Publishing Corporation (2) (12)	Newspaper	Senior Debt		20,759	20,759
		Subordinated Debt		20,405	20,405
		Preferred Stock	100 0%	7,999	8,730
		Common Stock	100.0%	365	145
Telecomm South, LLC (6)	Telecommunications	Senior Debt		2,961	859
		LLC Interest	100 0%	11	—
UMAC, Inc. (6)	Publishing	Common Stock	100.0%	10,183	181

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	September 30, 2004 Cost		Fair Value
Working Mother Media, Inc. (6)	Publishing	Senior Debt	$	7,526	$	7,526
		Class A Preferred Stock	99.2 %	11,497		4,294
		Class B Preferred Stock	100.0 %	1		—
		Class C Preferred Stock	100.0 %	1		—
		Common Stock	51.0 %	1		—
		Guaranty ($1,280)				
Total Control investments: Majority-owned				217,382		184,116
Total Investments				847,455		817,891
Unearned income				(13,216)		(13,216)
Total Investments net of unearned income			$	834,239	$	804,675

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003	
				Cost	Fair Value
Non-affiliate investments (less than 5% owned):					
21st Century Newspapers, Inc	Newspaper	Subordinated Debt		$ 22,266	$ 22,266
		Common Stock	1.0 %	453	667
aaiPharma Inc	Drugs	Senior Debt		4,875	4,875
The Adrenaline Group, Inc. (6)	Technology	Common Stock	2.7 %	—	4
American Consolidated Media Inc. (2)	Newspaper	Senior Debt		19,300	19,300
Auto Europe, LLC	Equipment Leasing	Senior Debt		10,000	10,000
Badoud Enterprises, Inc. (2)	Newspaper	Senior Debt		7,675	7,675
Barcom Electronic Inc.	Security Alarm	Senior Debt		3,393	3,393
Boucher Communications, Inc. (2)	Publishing	Senior Debt		1,400	1,400
		Stock Appreciation Rights		—	340
Bridgecom Holdings, Inc. (2) (11)	Telecommunications	Senior Debt		22,114	22,114
		Warrants to purchase Common Stock	13.0 %	2,122	4,364
Brookings Newspapers, L.L.C. (2)	Newspaper	Senior Debt		2,700	2,700
Cambridge Information Group, Inc (2)	Information Services	Senior Debt		15,450	15,450
CCG Consulting, LLC	Business Services	Senior Debt		1,451	1,451
		Warrants to purchase membership interest in LLC	21.5 %	—	—
Community Media Group, Inc. (2)	Newspaper	Senior Debt		10,345	10,345
Connective Corp (6) (15)	Leisure Goods	Common Stock	0.2 %	57	25
Creative Loafing, Inc (2)	Newspaper	Senior Debt		14,050	14,050
Crescent Publishing Company LLC (2)	Newspaper	Senior Debt		14,304	14,304

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	Fair Value
Cruz Bay Publishing, Inc. (2)	Publishing	Senior Debt		$ 6,200	$ 6,200
		Subordinated Debt		4,035	4,035
Dakota Imaging, Inc.	Technology	Senior Debt		7,062	7,062
		Warrants to purchase Common Stock	9.4 %	1,586	1,671
dick clark productions, inc.	Broadcasting	Subordinated Debt		16,479	16,479
		Warrants to purchase Common Stock	5.6%	858	639
		Common Stock	0 4 %	150	49
Dowden Health Media, Inc.	Publishing	Senior Debt		700	700
The e-Media Club, LLC(6)	Investment Fund	LLC Interest	0.8 %	88	27
FTI Technologies Holdings, Inc. (2)	Technology	Senior Debt		22,450	22,450
		Warrants to purchase Common Stock	4.2 %	—	—
Graycom, LLC (6)	Telecommunications	Warrants to purchase membership interest in LLC	27.8 %	71	74
Hometown Telephone, LLC (6)	Telecommunications	Warrants to purchase membership interest in LLC	27.8 %	—	—
I-55 Internet Services, Inc.	Telecommunications	Senior Debt		2,301	2,301
		Warrants to purchase Common Stock	7.5 %	103	156
IDS Telcom LLC	Telecommunications	Senior Debt		18,823	18,823
		Warrants to purchase membership interest in LLC	27.8 %	2,693	3,101
Images.com, Inc.	Information Services	Senior Debt		3,188	1,722
Information Today, Inc.(2)	Information Services	Senior Debt		9,192	9,192
Jeffrey A. Stern (6)	Other	Senior Debt		50	50

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	December 31, 2003 Fair Value
The Joseph F. Biddle Publishing Company (2)	Newspaper	Senior Debt		$ 10,305	$ 10,305
Joseph C. Millstone	Telecommunications	Senior Debt		500	500
The Korea Times Los Angeles, Inc.	Newspaper	Senior Debt		10,602	10,602
Manhattan Telecommunications Corporation (2)	Telecommunications	Senior Debt		13,925	13,925
		Subordinated Debt		12,328	12,328
		Preferred Stock	100.0 %	1,800	1,854
		Warrants to purchase Common Stock	28.0 %	2,805	4,021
Marketron International, Inc. (6) (8)	Business Services	Warrants to purchase Common Stock	1.5 %	—	—
McGinnis-Johnson Consulting, LLC (2)	Newspaper	Subordinated Debt		10,531	10,531
The Meow Mix Company	Food Products	Senior Debt		4,969	4,969
Midwest Towers Partners, LLC (2)	Telecommunications	Senior Debt		17,009	17,009
Miles Media Group, Inc. (2)	Publishing	Senior Debt		7,906	7,906
		Warrants to purchase Common Stock	12.4 %	21	21
Minnesota Publishers, Inc. (2)	Newspaper	Senior Debt		14,250	14,250
New Century Companies, Inc (6)	Industrial Equipment	Common Stock	2.3 %	157	144
		Warrants to purchase Common Stock	0.4 %	—	—
New Vision Broadcasting, LLC (2)	Broadcasting	Senior Debt		13,367	13,367
New Wave Communications, LLC(2)	Cable	Senior Debt		8,804	8,804

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	Fair Value
nii communications, inc. (2)	Telecommunications	Senior Debt		$ 7,353	$ 7,353
		Common Stock	3.0 %	400	137
		Warrants to purchase Common Stock	38.5 %	1,218	1,501
NOW Communications, Inc. (2)	Telecommunications	Senior Debt		4,783	4,125
		Warrants to purchase Common Stock	10.0 %	—	—
Pacific-Sierra Publishing, Inc.	Newspaper	Senior Debt		25,734	25,734
Powercom Corporation (2)	Telecommunications	Senior Debt		2,160	2,160
		Warrants to purchase Class A Common Stock	18.6 %	263	211
R.R. Bowker LLC (2)	Information Services	Senior Debt		9,500	9,500
		Warrants to purchase membership interest in LLC	14.0 %	882	1,434
Robert N. Snyder	Information Services	Senior Debt		1,300	1,300
Stonebridge Press, Inc. (2)	Newspaper	Senior Debt		5,466	5,466
SXC Health Solutions, Inc (2) (13)	Technology	Senior Debt		7,600	7,600
Talk America Holdings, Inc. (6)	Telecommunications	Common Stock	0.8 %	499	2,484
		Warrants to purchase Common Stock	0.8 %	25	474
TGI Group, LLC	Information Services	Senior Debt		6,225	6,225
		Warrants to purchase membership interest in LLC	5.0 %	126	—
Tower Resource Management, Inc.	Telecommunications	Senior Debt		1,503	1,503
		Warrants to purchase Common Stock	8.9 %	—	—

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	Fair Value
VS&A-PBI Holding LLC(6)	Publishing	LLC Interest	0.8%	$ 500	$ —
Wicks Business Information, LLC	Publishing	Unsecured Note		200	200
Wiesner Publishing Company, LLC (2)	Publishing	Senior Debt		5,461	5,461
		Subordinated Debt		5,623	5,623
		Warrants to purchase membership interest in LLC	15.0%	406	398
WirelessLines II, Inc	Telecommunications	Senior Debt		437	437
Witter Publishing Co., Inc	Publishing	Senior Debt		2,340	2,340
		Warrants to purchase Common Stock	10.5%	87	78
Wyoming Newspapers, Inc. (2)	Newspaper	Senior Debt		10,378	10,378
Total Non-affiliate investments				477,732	482,112
Affiliate investments (3):					
All Island Media, Inc.	Newspaper	Senior Debt		8,000	8,000
		Common Stock	9.1%	500	500
Country Media, Inc.	Newspaper	Senior Debt		7,176	7,176
		Common Stock	6 3%	100	134
Creatas, L.L.C. (2)	Information Services	Senior Debt		17,735	17,735
		Investor Class LLC Interest Guaranty ($501)	100.0%	1,273	2,951
Executive Enterprise Institute, LLC (6)	Business Services	LLC Interest	10 0%	301	—
Netplexus Corporation (2) (6)	Technology	Senior Debt		1,817	170
		Preferred Stock	51 0%	766	—
		Warrants to purchase Class A Common Stock	4.8%	—	—

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	December 31, 2003 Fair Value
Sunshine Media Delaware, LLC (2)	Publishing	Senior Debt		$ 12,839	$ 12,516
		Class A LLC Interest	12.8 %	564	—
		Warrants to purchase Class B LLC interest	100.0 %	—	—
ViewTrust Technology (6)	Technology	Common Stock	7.5 %	1	1
Total Affiliate investments				51,072	49,183
Control investments: Non-majority-owned (4):					
ETC Group, LLC (10)	Publishing	Senior Debt		1,200	1,200
		Series A LLC Interest	100.0 %	650	650
		Series C LLC Interest	100.0 %	100	100
Fawcette Technical Publications Holding (2)	Publishing	Senior Debt		12,160	12,160
		Subordinated Debt		3,906	3,906
		Series A Preferred Stock	100.0 %	2,569	718
		Common Stock	36.0 %	—	—
National Systems Integration, Inc. (9)	Security Alarm	Senior Debt		500	500
		Class B-2 Preferred Stock	100.0 %	4,409	3,833
		Common Stock	46.0 %	—	—
Platinum Wireless, Inc	Telecommunications	Senior Debt		875	875
		Common Stock	37.0 %	4,640	4,519
		Options to purchase Common Stock	1.5 %	272	98
Total Control investments: Non-majority-owned				31,281	28,559

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Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	December 31, 2003 Fair Value
Control investments: Majority-owned (5):					
AMI	Telecommunications	Senior Debt		$ 3,100	$ 237
Telecommunications Corporation (2) (6)		Series A-1 Preferred Stock	82.3 %	700	—
		Series A-2 Preferred Stock	100.0 %	1,995	—
		Series A-3 Preferred Stock	37.5 %	1,100	—
		Common Stock	5.1 %	200	—
Biznessonline.com, Inc. (2) (14)	Telecommunications	Senior Debt		18,556	18,556
		Preferred Stock	100.0 %	4,864	—
		Common Stock	73.2 %	540	—
Copperstate Technologies, Inc.	Security Alarm	Senior Debt		910	910
		Class A Common Stock	93.0 %	2,000	2,160
		Class B Common Stock	0.1 %	—	1
		Warrants to purchase Class B Common Stock	99.9 %	—	1,343
Corporate Legal Times L.L.C.	Publishing	Senior Debt		4,624	4,302
		Subordinated Debt		1,340	—
		LLC Interest	90.6 %	313	—
Crystal Media Network, LLC (7)	Broadcasting	LLC Interest	100.0 %	6,132	5,149
Interactive Business Solutions, Inc.	Security Alarm	Senior Debt		75	75
		Common Stock	100.0 %	2,750	1,351
Superior Publishing Corporation. (2) (15)	Newspaper	Senior Debt		20,760	20,760
		Subordinated Debt		28,000	28,000
		Preferred Stock	100.0 %	7,999	7,999
		Common Stock	100.0 %	1	1
Telecomm North	Telecommunications	Preferred Stock	100.0 %	31,856	31,856

Corp. (11)		Common Stock	100.0 %	—	—
Telecomm South, LLC (6)	Telecommunications	Senior Debt		3,292	2,210
		LLC Interest	100.0 %	10	—

See notes to consolidated financial statements (unaudited).

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MCG Capital Corporation

Consolidated Schedule of Investments (unaudited)

December 31, 2003

(dollars in thousands)

Portfolio Company	Industry	Title of Securities Held by the Company	Percentage of Class Held on a Fully Diluted Basis (1)	December 31, 2003 Cost	Fair Value
UMAC, Inc. (6)	Publishing	Common Stock	100.0 %	$ 10,375	$ 344
Working Mother Media, Inc. (6)	Publishing	Senior Debt		8,026	8,026
		Class A Preferred Stock	98.8 %	8,497	5,808
		Class B Preferred Stock	100.0 %	1	—
		Class C Preferred Stock	100.0 %	1	—
		Common Stock	51.0 %	1	—
Total Control investments: Majority-owned				168,018	139,088
Total Investments				728,103	698,942
Unearned income				(16,416)	(16,416)
Total Investments net of unearned income				$ 711,687	$ 682,526

(1) The "percentage of class held on a fully diluted basis" represents the percentage of the class of security we may own assuming we exercise our warrants or options (whether or not they are in-the-money) and assuming that warrants, options or convertible securities held by others are not exercised or converted. We have not included any security which is subject to significant vesting contingencies. Common stock, preferred stock, warrants, options and equity interests are generally non-income producing and restricted The percentage was calculated based on the most current outstanding share information available to us (i) in the case of private companies, provided by that company, and (ii) in the case of public companies, provided in that company's most recent public filings with the SEC.

(2) Some of the securities listed are issued by affiliate(s) of the listed portfolio company.

(3) Affiliate investments are generally defined under the Investment Company Act of 1940 as companies in which MCG owns at least 5% but not more than 25% of the voting securities of the company.

(4) Non-majority owned control investments are generally defined under the Investment Company Act of 1940 as companies in which MCG owns more than 25% but not more than 50% of the voting securities of the company.

(5) Majority owned investments are generally defined under the Investment Company Act of 1940 as companies in which MCG owns more than 50% of the voting securities of the company.

(6) Non-income producing at the relevant period end.

(7) In February 2003, we acquired the assets of NBG Radio Networks, Inc. in satisfaction of debt. The assets are held and operated through Crystal Media Network, LLC, which is a wholly owned portfolio company of MCG Capital Corporation.

(8) In February 2003, BuyMedia Inc. changed its name to Marketron International, Inc

(9) In March 2003, we converted $8,631 of senior debt and $1,262 of debtor in possession financing in Intellisec Holdings, Inc., into preferred and common stock in connection with a plan of reorganization. In March 2003, Intellisec Holdings, Inc changed its name to National Systems Integration, Inc. In June 2004, National Systems Integration, Inc. ceased operations and filed for protection under Chapter 7 of the United States Bankruptcy Code

See notes to consolidated financial statements (unaudited).

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(10) In July 2003, we acquired the assets of THE Journal LLC in satisfaction of debt and transferred those assets to a wholly owned subsidiary, ETC Group, LLC. In August 2003, we sold 50% of the equity in ETC Group, LLC to third party investors.

(11) In December 2003, Telecomm North Corp., a wholly owned portfolio company, entered into an agreement to merge with another of our portfolio companies, Bridgecom Holdings, Inc. The merger was completed in March 2004 with Bridgecom Holdings, Inc. as the surviving corporation.

(12) In December 2003, Superior Publishing Inc., a wholly owned portfolio company, purchased the stock of one of our portfolio companies, Murphy McGinnis Media, Inc.

(13) In July 2003, Systems Xcellence USA, Inc. changed its name to SXC Health Solutions, Inc.

(14) In February, 2004, BiznessOnline.com, Inc. changed its name to ClearTel Communications, Inc

(15) In April, 2004, Connective Corp. changed its name to Majesco Holdings Inc.

See notes to consolidated financial statements (unaudited).

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MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited)

(in thousands except share and per share amounts).

Note 1.Description of Business and Unaudited Interim Consolidated Financial Statements Basis of Presentation

MCG Capital Corporation ("MCG" or the "Company" or "we" or "us" or "our") is a solutions-focused financial services company providing financing and advisory services to a variety of small- and medium-sized companies throughout the United States with a focus on growth oriented companies. Currently, our portfolio consists primarily of companies in the communications, information services, media and technology, including software and technology-enabled business services, industry sectors. Our capital is generally used by our portfolio companies to finance acquisitions, recapitalizations, management buyouts, organic growth and working capital. Prior to its name change effective June 14, 2001, the Company's legal name was MCG Credit Corporation. The Company is a non-diversified internally managed, closed-end investment company that has elected to be treated as a business development company under the Investment Company Act of 1940, as amended ("1940 Act").

On March 3, 2004, MCG filed a Form N-2 Registration Statement with the Securities and Exchange Commission ("SEC") which allows MCG to offer, from time to time, 6,320,896 shares of common stock in one or more offerings and allows certain selling shareholders named therein to offer, from time to time, up to 11,679,104 shares of common stock in one or more offerings In connection with this Registration Statement, on May 26, 2004 MCG raised $56,250 of gross proceeds by selling 3,750,000 shares of common stock at an offering price of $15 00 per share On June 8, 2004, the underwriters in the May 26, 2004 offering exercised their over-allotment option and purchased an additional 562,500 shares of common stock at an offering price of $15.00 per share. As a result of the underwriters exercising their over-allotment, MCG raised an additional $8,438 of gross proceeds. Also in connection with this Registration Statement, on September 21, 2004, MCG raised $35,388 of gross proceeds by selling 2,008,396 shares of common stock at an offering price of $17.62 per share. On September 29, 2004, the underwriters in the September 21, 2004 offering exercised their over-allotment option and purchased an additional 301,259 shares of common stock at an offering price of $17.62 per share, which were registered on a registration statement on Form N-2 filed on September 16, 2004. As a result of the underwriters exercising their over-allotment, MCG raised an additional $5,308 of gross proceeds.

Interim consolidated financial statements of MCG are prepared in accordance with generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual consolidated financial statements prepared in accordance with GAAP are omitted. In the opinion of management, all adjustments, consisting solely of normal recurring accruals, considered necessary for the fair presentation of financial statements for the interim periods, have been included. The current period's results of operations are not necessarily indicative of results that ultimately may be achieved for the year The interim unaudited consolidated financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in the Company's Form 10-K for the fiscal year ended December 31, 2003, as filed with the SEC.

The accompanying financial statements reflect the consolidated accounts of MCG, including MCG-Kagan Research, Inc. and MCG's special purpose financing subsidiaries, MCG Finance I, LLC, MCG Finance II, LLC, MCG Finance III, LLC, MCG Finance IV, LLC, and MCG Finance V, LLC, with all significant intercompany balances eliminated, and the related consolidated results of operations. In accordance with Article 6 of Regulation S-X under the Securities Act of 1933 and Securities Exchange Act of 1934, the Company does not consolidate portfolio company investments, including those in which it has a controlling interest

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MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

Note 2.Investments

As of September 30, 2004 and December 31, 2003, investments consisted of the following:

	September 30, 2004		December 31, 2003	
	Cost	Fair Value	Cost	Fair Value
Commercial loans	$ 718,500	$ 709,041	$ 615,253	$ 605,551
Investments in equity securities	128,955	108,850	112,850	93,391
Unearned income	(13,216)	(13,216)	(16,416)	(16,416)
Total	$ 834,239	$ 804,675	$ 711,687	$ 682,526

MCG's customer base includes primarily small- and medium-sized private companies in the communications, information services, media and technology, including software and technology-enabled business services, industry sectors. The proceeds of the loans to these companies are generally used for buyouts, growth, acquisitions, liquidity, refinancings and restructurings. In addition, we have occasionally made loans to individuals who are principals in these companies where the proceeds are used for or in connection with the operations or capitalization of such companies. Our debt instruments generally provide for a contractual variable interest rate generally ranging from approximately 4% to 14%, a portion of which may be deferred. At September 30, 2004, approximately 90% of loans in the portfolio, based on amounts outstanding at cost, were at variable rates determined on the basis of a benchmark LIBOR or prime rate and approximately 10% were at fixed rates. In addition, approximately 52% of the loan portfolio has floors of between 1.25% and 3% on the LIBOR base index. The Company's loans generally have stated maturities at origination that range from 2 to 8 years. Customers typically pay an origination fee based on a percentage of the commitment amount. They also often pay a fee based on any undrawn commitments.

At September 30, 2004, approximately 38% of MCG's loans had detachable warrants or an option to purchase warrants, stock appreciation rights or other equity interests or other provisions designed to provide the Company with an enhanced internal rate of return through the potential recognition of capital gains from the sale of such interests. In lieu of cash for loan origination fees, MCG received warrants valued at $2,302 and $9,221 for the nine months ended September 30, 2004 and 2003, respectively. These equity and equity-like instruments generally do not produce a current return, but are held for potential investment appreciation and capital gains. The warrants and options to purchase warrants typically are exercisable immediately and typically remain exercisable for 10 years. The exercise prices on the warrants vary from nominal exercise prices to exercise prices that are at or above the current fair market value of the equity for which we are receiving warrants The equity interests and warrants and options to purchase warrants often include registration rights, which allow us, under certain circumstances, to require the portfolio company to register the underlying securities with the SEC after the portfolio company's initial public offering. Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the Consolidated Statements of Operations.

MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

The composition of MCG's investments as of September 30, 2004 and December 31, 2003 at cost and fair value was as follows (excluding unearned income):

	September 30, 2004		December 31, 2003	
	Investments at Cost	Percentage of Total Portfolio	Investments at Cost	Percentage of Total Portfolio
Senior Debt	$ 593,020	70.0 %	$ 510,545	70.1 %
Subordinated Debt	125,480	14.8 %	104,708	14.4 %
Equity	119,375	14.1 %	99,312	13.6 %
Warrants to Acquire Equity	9,580	1.1 %	13,538	1.9 %
Equity Appreciation Rights	—	0.0 %	—	0.0 %
Total	$ 847,455	100.0 %	$ 728,103	100.0 %

	September 30, 2004		December 31, 2003	
	Investments at Fair Value	Percentage of Total Portfolio	Investments at Fair Value	Percentage of Total Portfolio
Senior Debt	$ 584,793	71.5 %	$ 502,183	71.9 %
Subordinated Debt	124,248	15.2 %	103,368	14.7 %
Equity	96,027	11.7 %	73,467	10.5 %
Warrants to Acquire Equity	12,436	1.5 %	19,584	2.8 %
Equity Appreciation Rights	387	0.1 %	340	0.1 %
Total	$ 817,891	100.0 %	$ 698,942	100.0 %

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MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

Set forth below are tables showing the composition of MCG's portfolio by industry sector (excluding unearned income) at cost and fair value as of September 30, 2004 and December 31, 2003:

	September 30, 2004		December 31, 2003	
	Investments at Cost	Percentage of Total Portfolio	Investments at Cost	Percentage of Total Portfolio
Media				
Newspaper	$ 179,263	21.2 %	$ 250,895	34.5 %
Publishing	110,442	13.0	102,045	14.0
Broadcasting	69,174	8.2	45,790	6.3
Other	31,470	3.7	—	—
Telecommunications	204,502	24.1	201,272	27.6
Other Diversified Sectors	130,917	15.4	64,871	8.9
Information Services	70,319	8.3	21,948	3.0
Technology	51,368	6.1	41,282	5.7
Total	$ 847,455	100.0 %	$ 728,103	100.0 %

	September 30, 2004		December 31, 2003	
	Investments at Fair Value	Percentage of Total Portfolio	Investments at Fair Value	Percentage of Total Portfolio
Media				
Newspaper	$ 179,826	22.0 %	$ 251,143	35.9 %
Publishing	84,538	10.3	84,432	12.1
Broadcasting	67,767	8.3	44,487	6.4
Other	31,470	3.9	—	—
Telecommunications	188,752	23.1	192,872	27.5
Other Diversified Sectors	130,985	16.0	65,509	9.4
Information Services	83,998	10.2	21,541	3.1
Technology	50,555	6.2	38,958	5.6
Total	$ 817,891	100.0 %	$ 698,942	100.0 %

At September 30, 2004, there were $45 of loans greater than 60 days past due compared to $4,175 of loans at December 31, 2003. At September 30, 2004, there were $11,998 of loans on non-accrual, including all $45 of the loans greater than 60 days past due. At December 31, 2003, there were $14,617 of loans on non-accrual, including $50 of the loans greater than 60 days past due.

Note 3.Borrowings

On September 30, 2004, MCG completed a $397,700 term debt securitization. In addition to funding continued growth, the proceeds from the transaction were used to repay all of the outstanding borrowings under its $200,000 secured warehouse facility with UBS AG and all of the outstanding borrowings under its $115,000 revolving credit facility with Wachovia Bank, National Association. In connection with these repayments, MCG terminated these two facilities In addition, on September 10, 2004, MCG entered into a $25,000 senior secured credit facility with Bayerische Hypo-und Vereinsbank, AG.

Term Securitization 2004-1 On September 30, 2004, MCG established MCG Commercial Loan Trust 2004-1 (the "2004-1 Trust"), which issued three classes of series 2004-1 Notes. The facility was structured to hold up to $397,700 of loans, however as of September 30, 2004 only $296,809 of loans had been funded. There is an additional $98,936 of cash held by the trustee as of September 30, 2004 to be used by the 2004-1 Trust to purchase additional loans from MCG within 150 days of closing. The facility is secured by all of the 2004-1

MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share data)

Trust's commercial loans, cash held for investment, and any loans subsequently sold to the 2004-1 Trust, which as of September 30, 2004 totaled $397,045. This facility is scheduled to terminate July 20, 2016 or sooner upon the full repayment of the Class A-1, Class A-2 and Class B Notes The Class A-1 Notes, Class A-2 Notes and Class B Notes are scheduled to be repaid as MCG receives principal collections on the underlying collateral

The 2004-1 Trust issued $250,500 of Class A-1 Notes rated Aaa/AAA, $31,500 of Class A-2 Notes rated Aa1/AAA, and $43,500 of Class B Notes rated A2/A as rated by Moody's and Fitch, respectively. As of September 30, 2004 $325,500 of the Series 2004-1 Notes were outstanding The Series 2004-1 Class A-1 Notes, Class A-2 Notes and Class B Notes bear interest of LIBOR plus 0.43%, 0 65%, and 1.30%, respectively.

Senior Secured Credit Facility On September 10, 2004, MCG entered into a $25,000 senior secured revolving credit facility with Bayerische Hypo-Und Vereinsbank, A G. New advances under the credit facility are at the discretion of the lender. The credit facility expires on September 10, 2005 and bears interest at LIBOR plus 2.00% or the prime rate plus 0.50%. The credit facility is secured by a first priority security interest in MCG Capital Corporation's tangible and intangible assets subject to certain excluded collateral and certain permitted other liens. The credit facility contains customary terms and conditions, including, without limitation, affirmative and negative covenants such as information reporting, minimum stockholders' equity and a negative pledge. The credit facility also contains customary events of default with customary cure and notice, including, without limitation, nonpayment misrepresentation in a material respect, breach of covenant, cross-default to other indebtedness, bankruptcy, change of control, change of management and material adverse change. As of September 30, 2004, MCG had $25,000 outstanding under the credit facility.

Warehouse Credit Facility On January 29, 2004, MCG's wholly owned, bankruptcy remote, special purpose indirect subsidiary, MCG Commercial Loan Trust 2003-1 entered into a $200,000 secured warehouse credit facility with an affiliate of UBS AG MCG used the warehouse credit facility to fund its origination and purchase of a diverse pool of loans, including broadly syndicated rated loans, which it securitized using an affiliate of the lender as the exclusive structurer and underwriter or placement agent. Advances under the credit facility bore interest at LIBOR plus 0 50%. The warehouse credit facility operated much like a revolving credit facility that is primarily secured by the loans acquired with the advances under the credit facility. On September 30, 2004, MCG paid off the warehouse credit facility with the proceeds from the Term Securitization 2004-1 and terminated the facility.

Term Securitization 2001-1 On December 27, 2001, MCG established the MCG Commercial Loan Trust 2001-1 (the "2001-1 Trust"), which issued two classes of Series 2001-1 Notes. The facility is secured by all of the 2001-1 Trust's commercial loans which were contributed by MCG and totaled $205,093 as of September 30, 2004 and $247,490 as of December 31, 2003. This facility is scheduled to terminate on February 20, 2013 or sooner upon full repayment of the Class A and Class B Notes. The Class A and Class B Notes are scheduled to be repaid as MCG receives principal collections on the underlying collateral.

The 2001-1 Trust issued $229,860 of Class A Notes rated AAA/Aaa/AAA, and $35,363 of Class B Notes rated A/A2/A as rated by Standard & Poor's, Moody's and Fitch, respectively. As of September 30, 2004, $85,580 of Class A Series 2001-1 Notes and $35,363 of Class B Series 2001-1 Notes were outstanding and as of December 31, 2003 $137,777 of Class A Series 2001-1 Notes and $35,363 of Class B Series 2001-1 Notes were outstanding. The Series 2001-1 Class A Notes bear interest of LIBOR plus 0.60% and Series 2001-1 Class B Notes bear interest of LIBOR plus 1 75%, and interest on both is payable quarterly.

Revolving Credit Facility As of June 1, 2000, MCG, through MCG Master Trust, established a revolving credit facility (the "Revolving Credit Facility"), which allowed MCG to issue up to $200,000 of Series 2000-1 Class A Notes (the "Series 2000-1 Notes" or "Series 2000-1 Class A Asset Backed Securities") On February 12, 2004, the Revolving Credit Facility was amended to, among other things, reduce MCG's borrowing capacity

MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

from $200,000 to $130,000 and reduce the interest rate from a commercial paper rate plus 3.0% to LIBOR plus 1.5%.

On September 30, 2004, MCG paid off the revolving credit facility with the proceeds from the Term Securitization 2004-1 and terminated the facility. As of December 31, 2003, there were $130,991 of the Series 2000-1 Notes outstanding with one investor. As of September 30, 2004 and December 31, 2003, MCG had no notes outstanding under a swingline credit facility (the "Swingline Notes"), which was part of the Revolving Credit Facility, that allowed MCG to borrow up to $25,000 as part of the $200,000 total facility limit for a period of up to four days The Revolving Credit Facility was secured by $194,308 of commercial loans as of December31, 2003.

Each debt facility except the Senior Secured Credit Facility are funded through bankruptcy remote, special purpose, wholly owned subsidiaries of ours and, therefore, their assets may not be available to our creditors.

Amounts outstanding under the Warehouse Credit Facility, Trust Notes, Revolving Credit Facility, and the Senior Secured Credit Facility as of September 30, 2004 and December 31, 2003 by interest rate benchmark were as follows:

	September30,2004	December31,2003
90-day LIBOR	471,443	173,140
Commercial Paper Rate	—	130,991
	$ 471,443	$ 304,131

The following is a summary of the borrowings for the three and nine months ended September 30, 2004 and 2003:

(dollars in thousands)	Maximum Outstanding	Average Outstanding	Weighted Average InterestRate	InterestRate atPeriod-End
As of September 30, 2004 and the three months then ended				
Term Securitization 2004-1	$ 325,500	$ 3,533	2.2 %	2.2 %
Trust Notes	142,963	125,491	2.4	2.0
Revolving Credit Facility	113,683	104,628	3.1	—
Warehouse Credit Facility	96,427	76,052	2.0	—
Senior Secured Credit Facility	25,000	4,620	3.9	3.9
Swingline Notes	—	—	—	—
As of September 30, 2003 and the three months then ended				
Trust Notes	$ 190,970	$ 186,383	2.0 %	1.9 %
Revolving Credit Facility	142,234	136,893	4.1	4.3
Swingline Notes	—	—	—	—
As of September 30, 2004 and the nine months then ended				
Term Securitization 2004-1	$ 325,500	$ 1,188	2.2 %	2.2 %
Trust Notes	173,140	144,614	2.1	2.0
Revolving Credit Facility	130,991	110,842	3.0	—

Warehouse Credit Facility	96,427	41,121	1.9	—
Senior Secured Credit Facility	25,000	1,551	3.9	3.9
Swingline Notes	—	—	—	—
As of September 30, 2003 and the nine months then ended				
Trust Notes	$ 240,120	$ 198,346	2.1 %	1.9 %
Revolving Credit Facility	148,325	139,080	3.0	4.3
Swingline Notes	—	—	—	—

MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

Subject to certain minimum equity restrictions and other covenants, including restrictions on which loans the Company may leverage as collateral, the unused amount under the Revolving Credit Facility totaled $0 and $69,009 at September 30, 2004 and December 31, 2003, respectively.

Note 4.Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per common share for the three and nine months ended September 30, 2004 and 2003:

(in thousands except per share amounts)	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Basic				
Net income	$ **8,803**	$ 9,913	$ **28,543**	$ 27,799
Weighted average common shares outstanding	**42,646**	32,878	**40,049**	31,033
Earnings per common share—basic	$ **0.21**	$ 0.30	$ **0.71**	$ 0.90
Diluted				
Net income	$ **8,803**	$ 9,913	$ **28,543**	$ 27,799
Weighted average common shares outstanding	**42,646**	32,878	**40,049**	31,033
Dilutive effect of restricted stock on which forfeiture provisions have not lapsed	**30**	28	**55**	9
Weighted average common shares outstanding and common stock equivalents	**42,676**	32,906	**40,104**	31,042
Earnings per common share—diluted	$ **0.21**	$ 0.30	$ **0.71**	$ 0.90

For purposes of calculating earnings per common share, unvested restricted common stock whose forfeiture provisions are solely based on passage of time are included in diluted earnings per common share based on the treasury stock method Unvested restricted common stock whose forfeiture provisions are based on performance criteria are included in diluted earnings per common share when it becomes probable such criteria will be met and is calculated using the treasury stock method.

Note 5.Employee Stock Plans

During the first quarter of 2004, as part of our review of executive compensation, our compensation committee waived the performance-based forfeiture restrictions and modified the time-based forfeiture provisions associated with the Tier III shares of certain of our executive officers through their respective amended and restated restricted stock agreements. As a result, we recorded additional paid-in-capital and unearned compensation—restricted stock of $11,570 and $(11,570), respectively, and we also recorded long-term incentive compensation expense of $4,003 during the first quarter. The net effect of these modifications was to decrease stockholders' equity by $4,003 MCG's total stock compensation expense would not have changed if SFAS No. 123 "Accounting for Stock-Based Compensation" was applied.

In addition, our compensation committee agreed to allow the restrictions on certain shares of restricted stock to lapse. As a result, the Tier I and Tier II shares held by certain of our executive officers will vest immediately upon full repayment of the loans that are secured by the restricted stock. As of September 30, 2004, none of these executives had repaid these loans and, therefore, there was no additional expense recorded during the quarter related to these modifications.

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MCG Capital Corporation

Notes To Consolidated Financial Statements (unaudited) (continued)

(in thousands except share and per share amounts).

Note 6.Financial Highlights

The following is a schedule of financial highlights for the nine months ended September 30, 2004 and 2003:

	Nine Months Ended September 30, 2004		Nine Months Ended September 30, 2003	
Per Share Data:				
Net asset value at beginning of period (1)	$	11.98	$	11.56
Net operating income before investment gains and losses (2)		0.90		1.11
Net realized losses on investments (2)		(0.18)		(0.63)
Net change in unrealized appreciation on investments (2)		(0.01)		0.42
Net income		0.71		0.90
Dividends declared		(1.26)		(1.23)
Antidilutive effect of stock offering on distributions		0.10		0.23
Antidilutive effect of distributions recorded as compensation expense (2)		0.04		0.05
Net decrease in stockholders' equity resulting from distributions		(1.12)		(0.95)
Issuance of shares		3.44		2.99
Dilutive effect of share issuances and unvested restricted stock		(3.05)		(2.60)
Net increase in shareholders' equity from restricted stock amortization (2)		0.22		0.09
Net increase in stockholders' equity relating to share issuances		0.61		0.48
Net asset value at end of period (1)	$	12.18	$	11.99
Per share market value at end of period	$	17.36	$	15.60
Total return (3)		-4.95 %		56.27 %
Shares outstanding at end of period		45,356		38,729
Ratio/Supplemental Data:				
Net assets at end of period	$	552,282	$	464,439
Ratio of operating expenses to average net assets (annualized)		9.07 %		8.33 %
Ratio of net operating income to average net assets (annualized)		9.77 %		12.08 %

(1) Based on total shares outstanding.

(2) Based on average shares outstanding.

(3) For 2004, total return equals the increase of the ending market value over the December 31, 2003 price of $19.59 per share plus dividends paid ($1.26 per share), divided by the beginning price. For 2003, total return equals the increase of the ending market value over the December 31, 2002 price of $10.77 per share plus dividends paid ($1.23 per share), divided by the beginning price. Total return is not annualized.

Report of Independent Registered Public Accounting Firm

We have reviewed the accompanying consolidated balance sheet of MCG Capital Corporation as of September 30, 2004, including the consolidated schedules of investments, and the related consolidated statements of operations for the three-month and nine-month periods ended September 30, 2004 and 2003 and the consolidated statements of stockholders' equity, and statements of cash flows for the nine-month periods ended September 30, 2004 and 2003. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated interim financial statements referred to above for them to be in conformity with U S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of MCG Capital Corporation as of December 31, 2003, including the consolidated schedules of investments, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended (not presented herein), and in our report dated March 10, 2004 we expressed an unqualified opinion on those consolidated financial statements In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2003, including the schedule of investments, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ERNST & YOUNG LLP

McLean, Virginia

October 29, 2004

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The information contained in this section should be read in conjunction with the Selected Financial Data, and our Consolidated Financial Statements and notes thereto appearing elsewhere in this Quarterly Report.

This Quarterly Report, including the Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements that involve substantial risks and uncertainties. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs, and our assumptions Words such as "anticipates", "expects", "intends", "plans", "believes", "seeks", and "estimates" and variations of these words and similar expressions are intended to identify forward-looking statements. These statements are not guarantees of future performance and are subject to risks, uncertainties, and other factors, some of which are beyond our control and difficult to predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking statements including without limitation:

- economic downturns or recessions may impair our customers' ability to repay our loans and increase our non-performing assets;
- economic downturns or recessions may disproportionately impact the industry sectors in which we concentrate, and such conditions may cause us to suffer losses in our portfolio and experience diminished demand for capital in these industry sectors;
- a contraction of available credit and/or an inability to access the equity markets could impair our lending and investment activities,
- interest rate volatility could adversely affect our results;
- the risks associated with the possible disruption in our operations due to terrorism, and
- the risks, uncertainties and other factors we identify from time to time in our filings with the Securities and Exchange Commission, including our Form 10-Ks, Form 10-Qs and Form 8-Ks

Although we believe that the assumptions on which these forward-looking statements are based are reasonable, any of those assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions also could be incorrect. In light of these and other uncertainties, the inclusion of forward-looking statements in this Quarterly Report should not be regarded as a representation by us that our plans and objectives will be achieved You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report We undertake no obligation to update any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

Overview

MCG Capital Corporation is a solutions-focused financial services company providing financing and advisory services to a variety of small and medium-sized companies throughout the United States with a focus on growth oriented companies. Currently, our portfolio consists primarily of companies in the communications, information services, media, and technology, including software and technology-enabled business services, industry sectors. Our capital is generally used by our portfolio companies to finance acquisitions, recapitalizations, management buyouts, organic growth and working capital. On December 4, 2001, we completed an initial public offering and became an internally managed, non-diversified, closed-end investment company that elected to be treated as a business development company under the Investment Company Act of 1940. MCG Capital Corporation elected to be treated for federal income tax purposes as a regulated investment company under the Internal Revenue Code with the filing of its federal corporate income tax return for 2002, which election was effective as of January 1, 2002. Pursuant to this election, we generally will not have to pay corporate-level taxes on any income we distribute to our stockholders as dividends, allowing us to substantially reduce or eliminate our corporate-level tax liability.

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Portfolio Composition and Asset Quality

Our primary business is lending to and investing in growth oriented private businesses, through investments in senior debt, subordinated debt and equity-based investments, including warrants and equity appreciation rights.

The total portfolio value of our investments was $817.9 million and $698.9 million at September 30, 2004 and December 31, 2003, respectively (exclusive of unearned income) During the first nine months of 2004 we made investments in 30 new portfolio companies, including companies in diversified sectors (sectors other than communications, information services, media and technology), totaling $203.3 million and several follow on investments in existing customers representing $79.5 million The increase in investments during 2003 and the first nine months of 2004 was primarily due to newly originated debt and equity investments. During 2003 a higher proportion of our new origination activity was in the form of equity securities, which included new investments of $44.1 million to control companies

Early pay-offs and sales of securities for the first nine months of 2004 totaled $113.9 million and were due primarily to pay-offs of $75.6 million from four portfolio companies in the newspaper industry, $20 5 million from three portfolio companies in the technology industry and $9 0 million from three portfolio companies in the telecommunications industry. Early pay-offs and sales of securities in 2003 totaled $108.1 million and were primarily due to pay-offs of $42.5 million from six companies in the publishing industry and $46 5 million from four companies in the broadcasting industry.

Total portfolio investment activity for the nine months ended September 30, 2004 and year ended December 31, 2003, was as follows (exclusive of unearned income):

(dollars in millions)		NineMonths Ended September30,2004		YearEnded December31,2003
Beginning Portfolio	$	**698.9**	$	688.9
Originations/Draws/Advances on Loans		**276.4**		115.3
Originations/Warrants Capitalized on Equity (a)		**27.6**		77.5
Gross Payments / Reductions (a)		**(63.5)**		(69.1)
Early Pay-offs/Sales of Securities		**(113.8)**		(108.1)
Realized Gains		**7.2**		4.7
Realized Losses		**(14.5)**		(24.3)
Unrealized Appreciation on Investments		**33.4**		35.1
Unrealized Depreciation on Investments		**(33.8)**		(21.1)
Ending Portfolio	$	**817.9**	$	698.9

(a) Included in these amounts is the conversion of $6 6 million and $21.4 million of debt to equity in connection with certain restructurings for the nine months ended September 30, 2004 and year ended December 31, 2003, respectively.

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The following table shows the fair value of our portfolio of investments by asset class as of September 30, 2004 and December 31, 2003 (excluding unearned income):

	September 30, 2004			December 31, 2003	
(dollars in millions)		Investments at Fair Value	Percentage of Total Portfolio	Investments at Fair Value	Percentage of Total Portfolio
Senior Debt	$	584.8	71.5 % $	502.2	71 9 %
Subordinated Debt		124.2	15.2	103.4	14.7
Equity		96.0	11.7	73.4	10 5
Warrants to Acquire Equity		12.5	1.5	19.6	2.8
Equity Appreciation Rights		0.4	0.1	0.3	0.1
	$	817.9	100.0 % $	698.9	100.0 %

Set forth below is a table showing the composition of MCG's portfolio by industry sector at fair value at September 30, 2004 and December 31, 2003 (excluding unearned income).

	September 30, 2004			December 31, 2003	
(dollars in millions)		Investments at Fair Value	Percentage of Total Portfolio	Investments at Fair Value	Percentage of Total Portfolio
Media					
Newspaper	$	179.8	22.0 % $	251.1	35.9 %
Publishing		84.5	10.3	84.4	12.1
Broadcasting		67.8	8.3	44.5	6 4
Other		31.5	3.9	—	—
Telecommunications		188.7	23.1	192.9	27 5
Other Diversified Sectors		131.0	16.0	21.5	3.1
Information Services		84.0	10.2	65.5	9.4
Technology		50.6	6.2	39.0	5.6
	$	817.9	100.0 % $	698.9	100 0 %

Asset Quality

Asset quality is generally a function of economic conditions, our underwriting and ongoing management of our investment portfolio. As a business development company, our loans and equity investments are carried at market value or, in the absence of market value, at fair value as determined by our board of directors in good faith on a quarterly basis. As of September 30, 2004 and December 31, 2003, net unrealized depreciation on investments totaled $29 6 million and $29.2 million, respectively. For additional information on the change in unrealized depreciation on investments, see the section entitled "Net Investment Gains and Losses".

In addition to various risk management and monitoring tools, we also use an investment rating system to characterize and monitor our expected level of returns on each investment in our portfolio We use the following 1 to 5 investment rating scale. Below is a description of the conditions associated with each investment rating:

Investment Rating	Summary Description
1	Capital gain expected or realized
2	Full return of principal and interest or dividend expected with customer performing in accordance with plan
3	Full return of principal and interest or dividend expected but customer requires closer monitoring
4	Some loss of interest or dividend expected but still expecting an overall positive internal rate of return on the investment
5	Loss of interest or dividend and some loss of principal investment expected which would result in an overall negative internal rate of return on the investment

The following table shows the distribution of our investments on the 1 to 5 investment rating scale at fair value as of September 30, 2004 and December 31, 2003 (excluding unearned income):

(dollars in millions)

	September 30, 2004			December 31, 2003	
Investment Rating		Investmentsat Fair Value	Percentageof TotalPortfolio	Investmentsat Fair Value	Percentageof TotalPortfolio
1	$	277.7 (1)	33.9 %$	234.5 (1)	33.5 %
2		330.2	40.4	255.4	36.5
3		149.6	18.3	161.9	23.2
4		58.7	7.2	38.8	5.6
5		1.7	0.2	8.3	1.2
	$	817.9	100.0 %$	698.9	100.0 %

(1) Of this amount, $25.1 million at September 30, 2004 and $7.6 million at December 31, 2003 relates to debt investments in loans for which we have already realized a gain through the sale of equity instruments. While these debt investments are still outstanding, all of the related equity instruments have already been sold at a gain and, therefore, we do not expect any further realized gain.

We monitor loan concentrations in our portfolio, both on an individual loan basis and on a sector or industry basis, to manage overall portfolio performance due to specific customer issues or specific industry issues. The increase in investments with a 2 rating was primarily due to origination activity during the first nine months of 2004 At September 30, 2004, of the investments with a 5 rating, $0.9 million were loans, all of which were on non-accrual. Of the investments with a 4 rating, $51.9 million were loans, of which $9.9 million were on non-accrual At December 31, 2003, of the investments with a 5 rating, $2.6 million were loans, all of which were on non-accrual Of the investments with a 4 rating, $32.3 million were loans, of which $12.0 million were on non-accrual. The increase in investments with a 4 rating during the first none months of 2004 is due primarily to the downgrade of one investment in the technology sector.

We monitor individual customer's financial trends in order to assess the appropriate course of action with respect to each customer and to evaluate overall portfolio quality We closely monitor the status and performance of each individual investment on a quarterly and, in some cases, a monthly or more frequent basis. Because we are a provider of long-term privately negotiated investment capital to growth-oriented companies and we actively manage our investments through our contract structure and corporate governance rights, we do not believe that contract exceptions such as breaches of contractual covenants or late delivery of financial statements are necessarily an indication of deterioration in the credit quality or the need to pursue remedies or an active workout of a portfolio investment.

When a loan becomes 90 days or more past due, or if we otherwise do not expect the customer to be able to service its debt and other obligations, we will, as a general matter, place the loan on non-accrual status and cease recognizing interest income on that loan until all principal has been paid However, we may make exceptions to this policy if the investment is well secured and in the process of collection.

At September 30, 2004 and December 31, 2003, there were $0.1 million and $4 2 million, respectively, of loans, or approximately 0.01% and 0 6%, respectively, of the investment portfolio, greater than 60 days past due. At September 30, 2004, $12.0 million of loans, including all of the loans greater than 60 days past due, were on non-accrual status, which represented 1.5% of the investment portfolio. At December 31, 2003, $14.6 million of loans, including $0 1 million of the loans greater than 60 days past due, were on non-accrual status, which represented 2.1% of the investment portfolio The non-accrual and past due loans at September 30, 2004 and December 31, 2003 primarily represented borrowers in the publishing, telecommunications and paging businesses. Portions of the trade publishing industry, which are dependent on financial, technology or telecommunications advertising, have experienced sluggish advertising revenue. Certain companies in the telecommunications industry have suffered from competitive pressure from low cost and prepaid cellular calling plans.

At September 30, 2004, of the $121.2 million of loans to our majority owned portfolio companies, $12 0 million were on non-accrual status. At December 31, 2003, of the $83.1 million of loans to our majority owned portfolio companies, $10.5 million were on non-accrual status. At September 30, 2004, of the $36.6 million of loans to our controlled non-majority owned portfolio companies, none were on non-accrual status. At December 31, 2003, of the $18 6 million of loans to our controlled non-majority owned portfolio companies, $3.9 million were on non-accrual status As of September 30, 2004, of the $52 3 million of loans to other affiliates, none were on non-accrual status As of December 31, 2003, of the $45.6 million of loans to other affiliates, $0.2 million were on non-accrual status.

When principal and interest on a loan is not paid within the applicable grace period, we will contact the customer for collection At that time, we will make a determination as to the extent of the problem, if any We will then pursue a commitment for immediate payment and if we have not already, we will begin to more actively monitor the investment We will formulate strategies to optimize the resolution process and will begin the process of restructuring the investment to better reflect the current financial performance of the customer. Such a restructuring may involve deferring payments of principal and interest, adjusting interest rates or warrant positions, imposing additional fees, amending financial or operating covenants or converting debt to equity. In general, in order to compensate us for any enhanced risk, we receive additional compensation from the customer in connection with a restructuring. During the process of monitoring a loan that is out of compliance, we will in appropriate circumstances send a notice of non-compliance outlining the specific defaults that have occurred and preserving our remedies, and initiate a review of the collateral. When a restructuring is not the most appropriate course of action, we may determine to pursue remedies available under our loan documents or at law to minimize any potential losses, including initiating foreclosure and/or liquidation proceedings

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Results of Operations

Comparison of the Three and Nine Months Ended September 30, 2004 and 2003

Operating Income

Operating income includes interest income on commercial loans, dividend income, advisory fees and other income. Interest income is comprised of commercial loan interest at contractual rates and upfront fees that are amortized into income over the life of the loan Most of our loans contain lending features that adjust the rate margin based on the financial and operating performance of the borrower, which generally occurs quarterly.

The change in operating income for the three and nine months ended September 30, 2004 compared to the same periods in 2003 is attributable to the following items:

(dollars in thousands)	ThreeMonthsEnded September 30, 2004 vs. 2003	NineMonthsEnded September 30, 2004 vs. 2003
Change due to:		
Increase in assets (a)	$ 2,456	$ 620
Change in LIBOR (a)	880	775
Change in spread (a)	(2,462)	(3,819)
Increase in loan fee and dividend income	1,619	5,615
Increase in advisory fees and other income	2,440	8,556
Total change in operating income	$ 4,933	$ 11,747

(a) The change in interest income due to change in LIBOR, change in spread and loan growth has been allocated in proportion to the relationship of the absolute dollar amount of the changes in each

Total operating income for the third quarter of 2004 was $24 8 million, an increase of $4.9 million or 25% compared to the third quarter of 2003. Total operating income is primarily comprised of interest and dividend income on investments. Interest and dividend income for the third quarter of 2004 was $20.2 million, an increase of $2 5 million or 14% compared to the third quarter of 2003. The increase was due to an increase in dividend income of approximately $1 3 million and an increase in interest income of approximately $1.2 million. The increase in dividend income was primarily related to dividends on preferred stock of one of our control investments, Bridgecom Holdings, Inc. The increase in interest income on loans was due primarily to growth in total loans and an increase in LIBOR partially offset by a decrease in the spread to LIBOR in our loan portfolio. The lower spread to LIBOR is primarily the result of a change in our investment mix, which includes an increase in the proportion of our portfolio that is in diversified sectors (including sectors other than communications, information services, media and technology) The loans in diversified sectors are generally lower risk and yield lower interest rates, which accounted for approximately $0.9 million of the change in spread. We have originated these loans to enhance our diversification to reduce overall portfolio risk and to achieve better execution on our debt financing. Further, because LIBOR increased during the third quarter of 2004, the spread to LIBOR on fixed rate loans and loans with LIBOR floors decreased. Advisory fees and other income increased $2 4 million from the third quarter of 2003 to the third quarter of 2004 due primarily to research revenues from our subsidiary Kagan Research, LLC, which we acquired in the first quarter of 2004, and management fees from one of our control investments, Bridgecom Holdings, Inc.

Total operating income for the first nine months of 2004 was $69.8 million, an increase of $11.7 million or 20% compared to the first nine months of 2003. Total operating income is primarily comprised of interest and dividend income on investments. Interest and dividend income of $57.4 million for the first nine months of 2004 increased 6% from the first nine months of 2003. An increase in dividend income was partially offset by a decrease in interest income on loans The increase in dividend income was primarily related to dividends on preferred stock of one of our control investments, Bridgecom Holdings, Inc The decrease in interest income on loans was due to a lower average spread to LIBOR on the loan portfolio partially offset by asset growth and an increase in LIBOR. The lower spread to LIBOR is primarily the result of a change in investment mix, which includes an increase in the proportion of our portfolio that is in diversified sectors. These loans generally are lower risk and yield lower interest rates, which accounted for approximately $2.1 million of the change in spread We have originated these loans to enhance our diversification to reduce overall portfolio risk and to achieve better execution on our debt financing Further, because LIBOR increased during the first nine months of 2004, the spread to LIBOR on fixed rate loans and loans with LIBOR floors decreased. Advisory fees and other income increased $8.6 million from the first nine months of 2003 to the first nine months of 2004 due to an increase in advisory services provided to new and existing customers compared to the prior year's period, research revenues from Kagan Research, LLC and management fees from one of our control investments, Bridgecom Holdings, Inc

Operating Expenses

Operating expenses include interest expense on borrowings, including amortization of deferred debt issuance costs, employee compensation, and general and administrative expenses.

The change in operating expenses for the three and nine months ended September 30, 2004 compared to the same periods in 2003 is attributable to the following items:

(dollars in thousands)		ThreeMonthsEnded September 30, 2004 vs. 2003		NineMonthsEnded September 30, 2004 vs. 2003
Change due to:				
Decrease in borrowings (a)	$	(74)	$	(718)
Change in LIBOR (a)		518		421
Change in spread (a)		(822)		(648)
Debt cost amortization		21		28
Salaries and benefits		1,710		3,897
Long-term incentive compensation		562		5,214
General and administrative expense		862		1,712
Total change in operating expense	$	2,777	$	9,906

(a) The change in interest expense due to decrease in borrowings, change in LIBOR, and change in spread has been allocated in proportion to the relationship of the absolute dollar amount of the changes in each.

Total operating expenses for the third quarter of 2004 were $10 9 million, an increase of $2.8 million or 34% compared to the third quarter of 2003. Total operating expenses for the first nine months of 2004 were $33.6 million, an increase of $9.9 million or 42% compared to the first nine months of 2003 Total operating expenses are comprised of three components: (1) interest expense, (2) salaries and benefits and general and administrative expenses, and (3) long-term incentive compensation.

Interest expense declined by 13% to $2.3 million in the third quarter of 2004 compared to $2.7 million in the third quarter of 2003 and interest expense declined by 12% to $6.5 million for the first nine months of 2004 compared to $7.4 million for the first nine months of 2003 The decrease in both periods is primarily attributable to a decrease in the spread to LIBOR and a decrease in average borrowings offset by an increase in LIBOR.

Salaries and benefits and general and administrative expenses increased 69% from $3.7 million in the third quarter of 2003 to $6.3 million in the third quarter of 2004. For the first nine months of 2004 compared to the same period in 2003, these expenses increased 49% from $11.5 million in 2003 to $17.1 million in 2004. For the third quarter of 2004, the increase in salaries and benefits and general and administrative expenses was due primarily to expenses associated with Kagan Research, LLC as well as an increase in salaries and benefits due to additional hires and one time expenses associated with these new employees The additional hires are part of an ongoing effort to grow our infrastructure in order to support our plans for future growth. For the year-to-date period the increase is primarily due to expenses associated with Kagan Research, LLC.

Long-term incentive compensation expense is made up of non-cash amortization of restricted stock awards granted in 2001 and the treatment of dividends on all shares securing employee loans as compensation. During the first quarter of 2004, our compensation committee waived the performance-based forfeiture restrictions and modified the time-based forfeiture provisions associated with the Tier III shares of certain of our executive officers. Long-term incentive compensation totaled $2 3 million and $10.0 million for the third quarter and first nine months of 2004, respectively, compared to $1 8 million and $4.8 million for the third quarter and first nine months of 2003, respectively. The increases in long-term incentive compensation are primarily due to the modification made during the first quarter of 2004.

Net Operating Income Before Investment Gains and Losses

Net operating income before investment gains and losses (NOI) for the quarter ended September 30, 2004 totaled $13 9 million, an increase of 18% compared with $11.7 million for the same quarter of 2003 NOI for the nine months ended September 30, 2004 totaled $36.2 million, an increase of 5% compared with $34 4 million for the nine months ended September 30, 2003.

Net Investment Gains and Losses

Net investment losses totaled ($5.1) million and ($7 7) million for the third quarter and first nine months of 2004, respectively, compared to ($1.8) million and ($6 6) million for the same respective periods of 2003. Net investment losses for the third quarter of 2004 were primarily attributable to depreciation on investments in the Publishing and Telecommunications industries partially offset by appreciation in the Information Services industry. Net investment losses for the first nine months of 2004 related primarily to losses and depreciation in the Telecommunications, Technology and Publishing industries partially offset by gains and appreciation in the Information Services industry. See the tables below for more detail on net investment gains and losses. Reversals of unrealized appreciation and depreciation occur when a gain or loss becomes realized.

The following table summarizes our realized gains and losses on investments for the three and nine months ended September 30, 2004 and 2003:

MCG Capital Corporation

Summary of Realized Gains and Losses on Investments

(dollars in thousands)

Portfolio Company	Sector	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Realized gains (losses) on loans					
VS&A-PBI Holding LLC	Publishing	$ —	$ —	$ —	$ (7,901)
National Systems Integration, Inc.	Telecommunications	—	—	—	(5,812)
FTI Technologies Holdings, Inc.	Technology	(1,592)	—	(4,125)	—
AMI Telecommunications Corporation	Telecommunications	—	—	(2,994)	(5,585)
Rising Tide Holdings, Inc.	Publishing	—	—	—	(2,675)
Netplexus Corporation	Technology	(1,765)	(48)	(1,765)	(48)
THE Journal, LLC	Publishing	—	(959)	—	(959)
ClearTel Communications, Inc.	Telecommunications	—	—	(669)	—
NBG Radio Network, Inc.	Broadcasting	—	—	—	(398)
aaiPharma Inc.	Other Diversified	—	—	(278)	—
Other		49	—	91	—
		(3,308)	(1,007)	(9,740)	(23,378)
Realized gains (losses) on equity investments					
AMI Telecommunications Corporation	Telecommunications	—	—	(3,995)	—
Talk America Holdings, Inc.	Telecommunications	—	1,858	—	2,690
21st Century Newspapers, Inc.	Newspaper	2,478	—	2,478	—
R.R. Bowker LLC	Information Services	—	—	2,268	—
Bridgecom Holdings, Inc.	Telecommunications	—	—	2,158	—
SXC Health Solutions, Inc.	Technology	—	1,679	—	1,679
Netplexus Corporation	Technology	(766)	—	(766)	—
Fawcette Technical Publications Holding	Publishing	—	(519)	—	(519)
Dakota Imaging, Inc	Technology	—	—	331	—
Other		1	53	1	53
		1,713	3,071	2,475	3,903
Net realized gains (losses) on investments		$ (1,595)	$ 2,064	$ (7,265)	$ (19,475)

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The following table summarizes the net change in our unrealized appreciation and depreciation on investments for the three and nine months ended September 30, 2004 and 2003:

MCG Capital Corporation

Summary of Net Change in Unrealized Appreciation and Depreciation on Investments

(dollars in thousands)

Portfolio Company	Sector	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Unrealized appreciation on loans					
Images.com, Inc.	Information Services	$ —	$ —	$ 1,466	$ —
Other		403	415	1,091	145
		403	415	2,557	145
Unrealized appreciation on equity investments					
Creatas, L.L.C	Information Services	4,917	—	12,002	1,779
Fawcette Technical Publications Holding	Publishing	—	—	1,025	—
Bridgecom Holdings, Inc	Telecommunications	—	331	662	1 442
NII Communications, Inc	Telecommunications	222	—	625	164
Manhatten Telecommunications Corporation	Telecommunications	478	—	618	42
Superior Publishing Corporation	Newspaper	—	—	510	—
Talk America Holdings, Inc	Telecommunications	—	82	—	2,593
Copperstate Technologies, Inc	Telecommunications	—	1,268	—	1,379
SXC Health Solutions, Inc	Technology	—	—	—	631
Other		593	537	1,263	629
		6,210	2,218	16,705	8,659
Unrealized appreciation on investments		6,613	2,633	19,262	8,804
Unrealized depreciation on loans					
FTI Technologies Holdings, Inc	Technology	(1,000)	—	(5,125)	—
Sunshine Media Delaware, LLC	Publishing	(311)	—	(3,619)	—
Telecomm South, LLC	Telecommunications	(172)	(497)	(1,019)	(463)
National Systems Integration, Inc	Telecommunications	—	—	(910)	—
Witter Publishing Co Inc	Publishing	(602)	—	(602)	—
AMI Telecommunications Corporation	Telecommunications	—	(1,143)	—	(2,863)
Images.com, Inc	Information Services	—	(37)	—	(858)
Netplexus Corporation	Technology	—	(32)	—	(679)
Corporate Legal Times L L.C	Publishing	—	(36)	—	(537)
NOW Communications, Inc	Telecommunications	—	(94)	—	(559)
Other		(178)	(234)	(332)	(501)
		(2,263)	(2,073)	(11,607)	(6,460)
Unrealized depreciation on equity investments					
Working Mother Media, Inc	Publishing	(3,470)	—	(4,514)	(1,041)
National Systems Integration, Inc	Telecommunications	—	(132)	(3,833)	(707)
ClearTel Communications, Inc	Telecommunications	(3,668)	—	(3,668)	—
Copperstate Technologies, Inc	Telecommunications	—	—	(2,292)	—

Talk America Holdings, Inc	Telecommunications	(651)	—	(1,719)	—
Interactive Business Solutions, Inc	Telecommunications	(150)	(480)	(777)	(750)
ETC Group, LLC	Publishing	—	—	(750)	—
AMI Telecommunications Corporation	Telecommunications	—	—	—	(2,695)
Fawcette Technical Publications Holding	Publishing	—	(1,328)	—	(1,437)
Crystal Media Network, LLC	Broadcasting	—	(983)	(347)	(983)
Biznessonline com, Inc	Telecommunications	—	—	—	(2,001)
Creatas, L L C	Information Services	—	(1,175)	—	—
Bridgecom Holdings, Inc	Telecommunications	(771)	—	—	—
Platinum Wireless, Inc	Telecommunications	—	(170)	—	(274)
Other		(889)	(437)	(749)	(1,070)
		(9,599)	(4,705)	(18,649)	(10,958)
Unrealized depreciation on investments		(11,862)	(6,778)	(30,256)	(17,418)

Portfolio Company	Sector	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003
Reversal of unrealized (appreciation) depreciation*					
AMI Telecommunications Corporation	Telecommunications	—	—	6,858	5,143
FTI Technologies Holdings, Inc	Technology	1,592	—	4,125	—
Netplexus Corporation	Technology	2,487	—	2,413	—
Bridgecom Holdings, Inc	Telecommunications	—	—	(2,242)	—
RR Bowker	Information Services	—	—	(794)	—
Dakota Imaging, Inc	Technology	—	—	(331)	—
21st Century Newspapers, Inc	Newspaper	(2,441)	—	(215)	—
Talk America Holdings, Inc	Telecommunications	—	(1,381)	—	(1,746)
THE Journal, LLC	Publishing	—	1,752	—	1,752
NBG Radio Network, Inc	Broadcasting	—	—	—	574
Rising Tide Holdings, Inc	Publishing	—	—	—	2,735
National Systems Integration, Inc	Telecommunications	—	—	—	5,276
VS&A-PBI Holding LLC	Publishing	—	—	—	7,901
SXC Health Solutions, Inc	Technology	—	(631)	—	(631)
NOW Communications, Inc	Telecommunications	—	—	658	—
Fawcette Technical Publications Holding	Publishing	—	519	—	519
Other		113	(5)	119	(5)
Total reversal of unrealized (appreciation) depreciation		1,751	254	10,591	21,518
Net change in unrealized depreciation on investments		$ (3,498)	$ (3,891)	$ (403)	$ 12,904

* When a gain or loss becomes realized, the prior unrealized appreciation or depreciation is reversed.

Net Income

Net income totaled $8 8 million for the quarter ended September 30, 2004 compared to $9.9 million for the quarter ended September 30, 2003. For the nine months ended September 30, 2004, net income totaled $28 5 million compared to $27.8 million for the same period in 2003. Earnings per share for the quarter ended September 30, 2004 decreased from $0.30 for the same period in 2003 to $0.21. Earnings per share decreased for the nine months ended September 30, 2004 from $0.90 for the same period in 2003 to $0.71. The decrease in earnings per share for the quarter and year to date is due primarily to a higher number of shares outstanding and a higher amount of net investment losses during the 2004 periods

Financial Condition, Liquidity and Capital Resources

Cash, Cash Equivalents and Cash, Securitization Accounts

At September 30, 2004 and December 31, 2003, we had $111 9 million and $60.1 million, respectively, in cash and cash equivalents In addition, at September 30, 2004 and December 31, 2003, we had $109.9 million and $33.4 million, respectively, in cash, securitization accounts. We invest cash on hand in interest bearing deposit accounts with daily sweep features Cash, securitization accounts includes amounts held in designated bank accounts representing payments received on securitized loans and balances available for origination of loans by MCG to complete the funding of the 2004-1 Term Securitization. We are required to use a portion of these amounts to pay interest expense, reduce borrowings, or pay other amounts in accordance with the related securitization agreements and to originate loans. As of September 30, 2004 and December 31, 2003, $98.9 million and $0 0 million, respectively, of the cash held in securitization accounts was available for originations of loans that meet certain requirements. Our objective is to maintain sufficient cash on hand to cover current funding requirements, operations and to maintain flexibility as we manage our debt facilities. Borrowed funds that have not yet been invested may negatively impact our earnings until they are invested since the interest we pay on borrowings typically exceeds the rate of return that we are able to earn on temporary cash investments.

For the first nine months of 2004, net cash provided by operating activities totaled $43.6 million, an increase of $14.1 million over the first nine months of 2003 This increase was due primarily to higher cash received on previously deferred payment-in-kind interest during the first nine months of 2004 as compared to the first nine months of 2003. In the first nine months of 2004, net cash provided in investing and financing activities totaled $8 2 million compared with $115.7 million in the first nine months of 2003. The 2004 activity was principally due to higher investment originations in 2004 more than offset by principal payments on loans, issuance of common stock and new debt.

Liquidity and Capital Resources

We expect our cash on hand and cash generated from operations, including the portion of the cash in securitization accounts that will be released to us, to be adequate to meet our cash needs at our current level of operations. We generally fund new originations using cash on hand, advances under our borrowing facilities and equity financings.

On March 3, 2004, we filed a registration statement on Form N-2 with the Securities and Exchange Commission which allows us to offer, from time to time, 6,320,896 shares of common stock in one or more offerings and allows certain selling shareholders named therein to offer, from time to time, up to 11,679,104 shares of common stock in one or more offerings. In connection with this Registration Statement, on May 26, 2004 we raised $56.3 million of gross proceeds by selling 3,750,000 shares of common stock at an offering price of $15.00 per share. On June 8, 2004, the underwriters in the May 26, 2004 offering exercised their over-allotment option and purchased an additional 562,500 shares of common stock at an offering price of $15.00 per share. As a result of the underwriters exercising their over-allotment, we raised an additional $8.4 million of gross proceeds. Also in connection with this Registration Statement, on September 21, 2004 we raised $35.4 million of gross proceeds by selling 2,008,396 shares of common stock at an offering price of $17.62 per share. On September 29, 2004, the underwriters in the September 21, 2004 offering exercised their over-allotment option and purchased an additional 301,259 shares of common stock at an offering price of $17.62 per share, which were registered on a registration statement on Form N-2 filed on September 16, 2004. As a result of the underwriters exercising their over-allotment, we raised an additional $5.3 million of gross proceeds.

In order to satisfy the requirements applicable to a regulated investment company, we intend to distribute to our stockholders all of our income except for certain net capital gains and adjustments for long-term incentive compensation. In addition, as a business development company, we generally will be required to meet a coverage ratio of total assets to total senior securities, which include all of our borrowings and any preferred stock we may issue in the future, of at least 200%. As of September 30, 2004, this ratio was 221%. This requirement limits the amount that we may borrow. To fund growth in our investment portfolio in the future, we anticipate needing to raise additional capital from various sources, including the equity markets and the securitization or other debt-related markets.

Off-Balance Sheet Arrangements

We are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financial needs of our customers. These instruments include commitments to extend credit and involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. We attempt to limit our credit risk by conducting extensive due diligence and obtaining collateral where appropriate.

As of September 30, 2004, we had unused commitments to extend credit to our customers of $31 6 million, which are not reflected on our balance sheet. See "Borrowings" section below for discussion of our borrowing facilities.

Contractual Obligations

The following table shows our significant contractual obligations as of September 30, 2004:

(dollars in millions)	Total	Lessthan 1 year	1-3 years	4-5 years	After 5years
			Payments Due by Period		
Contractual Obligations (a)					
Borrowings (b)	$ 471.4	$ 55 0	$ 90.9	$ —	$ 325.50
Future minimum rental obligations	13.3	1.5	3.1	3.2	5.5
Total contractual obligations	$ 484.7	$ 56.5	$ 94.0	$ 3.2	$ 331.0

(a) This excludes the unused commitments to extend credit to our customers of $31.6 million as discussed above.

(b) Borrowings under the Warehouse Credit Facility and the Revolving Credit Facility are listed based on the contractual maturity of the respective facility due to the revolving nature of the facilities. Repayments of the Series 2001-1 Notes are based on the contractual principal collections of the loans which comprise the collateral. Repayments of the Series 2004-1 Notes are based on the contractual maturity of the facility because the required payments are based on principal collections of the loans that comprise the collateral, but the final pool of collateral my change within 150 days of closing. Actual repayments could differ significantly due to prepayments by our borrowers and modifications of our borrowers' existing loan agreements.

Borrowings

On September 30, 2004, we completed a $397.7 million term debt securitization. In addition to funding continued growth, the proceeds from the transaction were used to repay all of the outstanding borrowings under our $200 million secured warehouse facility, MCG Commercial Loan Trust 2003-1, with UBS AG and all of the outstanding borrowings under our $115 million revolving credit facility with Wachovia Bank, National Association. In connection with these repayments, we terminated these two facilities. In addition, on September10, 2004, we entered into a $25 0 million senior secured credit facility with Bayerische Hypo-und Vereinsbank, AG.

Term Securitization 2004-1 On September 30, 2004, we established MCG Commercial Loan Trust 2004-1 (the "2004-1 Trust"), which issued three classes of series 2004-1 Notes. The facility was structured to hold up to $397.7 million of loans, however as of September 30, 2004 only $296 8 million of loans had been funded. There is an additional $98 9 million of cash held by the trustee as of September 30, 2004 to be used by the 2004-1 Trust to purchase additional loans from us within 150 days of closing The facility is secured by all of the 2004-1 Trust's commercial loans, cash held for investment, and any loans subsequently sold to the 2004-1 Trust, which as of September 30, 2004 totaled $397.0 million This facility is scheduled to terminate July 20, 2016 or sooner upon the full repayment of the Class A-1, Class A-2 and Class B Notes. The Class A-1 Notes, Class A-2 Notes and Class B Notes are scheduled to be repaid as we receive principal collections on the underlying collateral

The 2004-1 Trust issued $250.5 million of Class A-1 Notes rated Aaa/AAA, $31.5 million of Class A-2 Notes rated Aa1/AAA, and $43.5 million of Class B Notes rated A2/A as rated by Moody's and Fitch, respectively. As of September 30, 2004 $325,500 of the Series 2004-1 Notes were outstanding. The Series 2004-1 Class A-1 Notes, Class A-2 Notes and Class B Notes bear interest of LIBOR plus 0 43%, 0.65%, and 1.30%, respectively.

Senior Secured Credit Facility On September 10, 2004, we entered into a $25.0 million senior secured revolving credit facility with Bayerische Hypo-Und Vereinsbank, A.G. New advances under the credit facility are at the discretion of the lender. The credit facility expires on September 10, 2005 and bears interest at LIBOR plus 2 00% or the prime rate plus 0.50%. The credit facility will be secured by a first priority security interest in our tangible and intangible assets subject to certain excluded collateral and certain permitted other liens. The credit facility contains customary terms and conditions, including, without limitation, affirmative and negative covenants such as information reporting, minimum stockholders' equity and a negative pledge. The credit facility also contains customary events of default with customary cure and notice, including, without limitation, nonpayment misrepresentation in a material respect, breach of covenant, cross-default to other indebtedness, bankruptcy, change of control, change of management and material adverse change. As of September 30, 2004, we had $25.0 million outstanding under the credit facility.

Warehouse Facility On January 29, 2004, our wholly owned, bankruptcy remote, special purpose indirect subsidiary, MCG Commercial Loan Trust 2003-1 entered into a $200 million secured warehouse credit facility with an affiliate of UBS AG. We used the warehouse credit facility to fund our origination and purchase of a diverse pool of loans, including broadly syndicated rated loans, which we securitized using an affiliate of the lender as the exclusive structurer and underwriter or placement agent. Advances under the credit facility bore interest at LIBOR plus 0.50%. The warehouse credit facility operated much like a revolving credit facility that is primarily secured by the loans acquired with the advances under the credit facility. On September 30, 2004, we paid off the warehouse credit facility with the proceeds from the Term Securitization 2004-1 and terminated the facility.

Term Securitization On December 27, 2001, we established the MCG Commercial Loan Trust 2001-1 (the "Trust"), which issued two classes of Series 2001-1 Notes. The facility is secured by all of the Trust's commercial loans which were contributed by us and totaled $205.1 million as of September 30, 2004 and $247.5 million as of December 31, 2003. This facility is scheduled to terminate on February 20, 2013 or sooner upon full repayment of the Class A and Class B Notes The Class A and Class B Notes are scheduled to be repaid as we receive principal collections on the underlying collateral.

The 2001-1 Trust issued $229 8 million of Class A Notes rated AAA/Aaa/AAA, and $35.4 million of Class B Notes rated A/A2/A (the "Series 2001-1 Class A Asset Backed Bonds" and "Series 2001-1 Class B Asset Backed Bonds") as rated by Standard & Poor's, Moody's and Fitch, respectively. As of September 30, 2004, $120.9 million of the Series 2001-1 Notes were outstanding and $173 1 million were outstanding as of December 31, 2003. The Series 2001-1 Class A Asset Backed Bonds bear interest of LIBOR plus 0.60% and Series 2001-1 Class B Asset Backed Bonds bear interest of LIBOR plus 1.75%, and interest on both is payable quarterly.

Revolving Credit Facility As of June 1, 2000, we, through MCG Master Trust, established a revolving credit facility (the "Revolving Credit Facility"), which allowed us to issue up to $200.0 million of Series 2000-1 Class A Notes (the "Series 2000-1 Notes" or "Series 2000-1 Class A Asset Backed Securities"). On February 12, 2004, the Revolving Credit Facility was amended to, among other things, reduce our borrowing capacity from $200.0 million to $130.0 million and reduce the interest rate from a commercial paper rate plus 3.0% to LIBOR plus 1.5%. On September 30, 2004, we paid off the revolving credit facility with the proceeds from the Term Securitization 2004-1 and terminated the facility. As of December 31, 2003, there were $130.0 million of the Series 2000-1 Notes outstanding with one investor. As of September 30, 2004 and December 31, 2003, we had no notes outstanding under a swingline credit facility (the "Swingline Notes"), which was part of the Revolving Credit Facility, that allowed us to borrow up to $25.0 million as part of the $200.0 million total facility limit for a period of up to four days. The Revolving Credit Facility was secured by $194.3 million of commercial loans as of December 31, 2003.

Each debt facility except the Senior Secured Credit Facility are funded through bankruptcy remote, special purpose, wholly owned subsidiaries of ours and, therefore, their assets may not be available to our creditors.

Outstanding Borrowings

At September 30, 2004, we had aggregate outstanding borrowings of $471.4 million. The following table shows the facility amounts and outstanding borrowings at September 30, 2004.

(dollars in millions)	Facility amount	Amount outstanding	Interest Rate(a)
Term Securitization			
Series 2004-1 Class A-1 Asset Backed Bonds	$ 250.5	$ 250.5	2.06 %
Series 2004-1 Class A-2 Asset Backed Bonds	31 5	31.5	2.28
Series 2004-1 Class B Asset Backed Bonds	43.5	43.5	2 93
Series 2001-1 Class A Asset Backed Bonds	85.5	85.5	2.23
Series 2001-1 Class B Asset Backed Bonds	35.4	35.4	3.38
Senior Secured Credit Facility	25.0	25.0	3.88
Total borrowings	$ 471 4	$ 471.4	2.38 %

(a) Excludes the cost of commitment fees and other facility fees.

At December 31, 2003, we had aggregate outstanding borrowings of $304 1 million. The following table shows the facility amounts and outstanding borrowings at December 31, 2003:

(dollars in millions)	Facility amount	Amount outstanding	Interest Rate(a)
Term Securitization			
Series 2001-1 Class A Asset Backed Bonds	$ 137.7	$ 137.7	1.77 %
Series 2001-1 Class B Asset Backed Bonds	35 4	35.4	2.92
Revolving Credit Facility			
Series 2000-1 Class A Asset Backed Securities	200.0	131.0	4.12
Total borrowings	$ 373.1	$ 304.1	2.91 %

(a) Excludes the cost of commitment fees and other facility fees.

Each of our borrowing facilities is funded through bankruptcy remote, special purpose, wholly-owned subsidiaries of ours and, therefore, their assets may not be available to our creditors. See Note 3 to the Consolidated Financial Statements for further discussion of our borrowings.

Dividends

We have elected to be taxed as a regulated investment company under Subchapter M of the Internal Revenue Code. In order to maintain our status as a regulated investment company, we are required to (i) distribute at least 90% of our investment company taxable income and 90% of any ordinary pre-RIC built in gains we recognize between January 1, 2002 and December 31, 2011, less any taxes due on those gains to avoid corporate level taxes on the amount distributed to stockholders (other than any built in gain recognized between January 1, 2002 and December 31, 2011) and (ii) distribute (actually or on a deemed basis) at least 98% of our income (both ordinary income and net capital gains) to avoid an excise tax. We intend to make distributions on a quarterly basis to our stockholders of all of our income, except for certain net capital gains and adjustments for long-term incentive compensation expense. We intend to make deemed distributions to our stockholders of any retained net capital gains.

We may not be able to achieve operating results that will allow us to make distributions at a specific level or to increase the amount of these distributions from time to time. In addition, we may be limited in our ability to make distributions due to the asset coverage test for borrowings applicable to us as a business development company under the Investment Company Act of 1940 and due to provisions in our credit facilities. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax consequences, including possible loss of our status as a regulated investment company. We cannot assure shareholders that they will receive any distributions or distributions at a particular level.

The following table summarizes our dividends declared and paid on all shares, including restricted stock, to date:

Date Declared	Record Date	Payment Date	Amount
October 29, 2004	November 19, 2004	January 27, 2005	0.42
July 28, 2004	August 20, 2004	October 28, 2004	0.42
April 22, 2004	May 7, 2004	July 29, 2004	0.42

March 25, 2004	April 6, 2004	April 29, 2004	0.42
December 16, 2003	December 31, 2003	January 29, 2004	0.42
August 6, 2003	August 18, 2003	October 30, 2003	0.42
June 16, 2003	June 23, 2003	July 30, 2003	0.41
March 28, 2003	April 16, 2003	April 29, 2003	0.40
December 18, 2002	December 30, 2002	January 30, 2003	0.42
September 30, 2002	October 16, 2002	October 30, 2002	0.46
June 3, 2002	June 11, 2002	July 31, 2002	0.47
March 28, 2002	April 17, 2002	April 30, 2002	0.41
December 31, 2001	January 22, 2002	January 31, 2002	0.86
Total Declared			$ 5.95

The aggregate dividend of $0.86 per share in December 2001 consisted of a dividend of $0.25 per share for the fourth quarter of 2001 and an additional dividend of $0.61 per share representing the distribution of substantially all of our earnings and profits since inception through December 31, 2001. The aggregate dividend of $0 46 declared in September 2002 consisted of a dividend of $0.43 per share for the third quarter of 2002 and an additional dividend of $0.03 per share which represented the remaining distribution of our earnings and profits since inception through December 31, 2001. The aggregate dividend declared in December 2001 along with the $0.03 dividend declared in September, 2002 were required for us to qualify as a regulated investment company.

Related Party Transactions

Prior to election to be regulated as a business development company, we terminated our stock option plan and adopted a restricted stock program under which we issued 1,539,851 shares of restricted common stock to employees and directors. The total number of shares issued for the termination of the option plan was based upon the Black-Scholes option-pricing model and assumptions and approved by our board of directors.

Additionally, in connection with the termination of our stock option plan, certain executive officers and employees purchased a portion of the 1,539,851 shares of restricted common stock at a per share price of $17.00 Those executive officers and employees issued partially non-recourse notes to us, with an aggregate face value of $5.8 million secured by approximately 1.4 million shares with a value of $23.8 million at the initial public offering price. The notes are payable at the end of a four and a half-year term, subject to acceleration, bear interest at 4.13% payable annually and are secured by all of the restricted common stock held by such employee and for some employees, for a specified time-period, additional shares of our common stock the employee owns. The notes are non-recourse as to the principal amount but recourse as to the interest. Amounts due on these loans are reflected as a reduction of stockholders' equity in the consolidated balance sheets.

In the first quarter of 2004, as part of a review of our executive compensation, the compensation committee of our Board of Directors agreed with certain of our executive officers to allow the forfeiture restrictions to lapse with respect to their Tier I and Tier II shares immediately upon full repayment of the partially nonrecourse promissory notes that are secured by the restricted stock. In addition, the compensation committee waived the performance-based forfeiture restrictions and modified the time-based forfeiture provisions associated with the Tier III shares through their respective amended and restated restricted stock agreements. The impact of these changes on long-term incentive compensation expense was an increase of approximately $4.1 million for the first quarter of 2004.

Critical Accounting Policies

The consolidated financial statements are based on the selection and application of significant accounting policies, which require management to make significant estimates and assumptions We believe that the following are some of the more critical judgment areas in the application of our accounting policies that currently affect our financial condition and results of operations.

Income Recognition

Interest on commercial loans is computed by methods that generally result in level rates of return on principal amounts outstanding. When a loan becomes 90 days or more past due, or if we otherwise do not expect the customer to be able to service its debt and other obligations, we will, as a general matter, place the loan on non-accrual status and cease recognizing interest income on that loan until all principal has been paid. However, we may make exceptions to this policy if the investment is well secured and in the process of collection.

Paid-in-Kind Interest

In accordance with GAAP, we include in income certain amounts that we have not yet received in cash, such as contractual paid-in-kind (PIK) interest, which represents contractually deferred interest added to the loan balance that is generally due at the end of the loan term However, in certain cases, a customer makes principal payments on its loan prior to making payments to reduce the PIK loan balances and, therefore, the PIK portion of a customer's loan can increase while the total outstanding amount of the loan to that customer may stay the same or decrease. PIK loans represented $14.9 million or 1.8% of our portfolio of investments as of September 30, 2004 and $27.3 million or 3 9% of our portfolio of investments as of December 31, 2003.

PIK related activity for the nine months ended September 30, 2004 and the year ended December 31, 2003 was as follows:

(in millions)		Nine Months Ended September 30, 2004		Year Ended December 31, 2003
Beginning PIK loan balance	$	27.3	$	27.2
PIK interest earned during the period		7.9		18.3
Change in interest receivable on PIK loans		—		0.1
Principal payments of cash on PIK loans		(12.3)		(7.0)
PIK loans converted to other securities		(7.9)		(10.9)
Realized loss		(0.1)		(0.4)
Ending PIK loan balance	$	14.9	$	27.3

As noted above, in certain cases, a customer may make principal payments on its loan that are contractually applied first to the non-PIK loan balance instead of the PIK loan balance. If all principal payments from these customers had been applied first to any PIK loan balance outstanding at the time of the payment, and any remainder applied to the non-PIK loan balance, an additional $5.5 million of payments would have been applied against the September 30, 2004 PIK loan balance of $14.9 million and an additional $6.6 million of payments would have been applied against the December 31, 2003 PIK loan balance of $27.3 million.

As of September 30, 2004, 90% of the $14 9 million of PIK loans outstanding have an investment rating of 3 or better and as of December 31, 2003, 93% of the $27.3 million of PIK loans outstanding had an investment rating of 3 or better. The net increase in loan balances as a result of contracted PIK arrangements is separately identified on our consolidated statements of cash flows.

Loan Origination Fees

Loan origination fees are deferred and amortized as adjustments to the related loan's yield over the contractual life of the loan. In certain loan arrangements, warrants or other equity interests are received from the borrower as additional origination fees. The borrowers granting these interests are typically non-publicly traded companies. We record the financial instruments received at fair value as determined by our board of directors. Fair values are determined using various valuation models which attempt to estimate the underlying value of the associated entity. These models are then applied to our ownership share considering any discounts for transfer restrictions or other terms which impact the value. Changes in these values are recorded through our statement of operations. Any resulting discount on the loan from recordation of warrant and other equity instruments are accreted into income over the term of the loan. We had $13.2 million and $16.4 million of unearned income as of September 30, 2004 and December 31, 2003, respectively.

Unearned fee activity for the nine months ended September 30, 2004 and year ended December 31, 2003 was as follows:

(in millions)	Nine Months Ended September 30, 2004			Year Ended December 31, 2003		
	Cash Received	Equity Interest and Future Receivables	Total	Cash Received	Equity Interest and Future Receivables	Total
Beginning unearned income balance	$ 5.6	$ 10.8	$ 16.4	$ 8.3	$ 4.5	$ 12 8
Additional fees	2.3	2.3	4.6	1.8	10.6	12.4
Unearned income recognized	(2.5)	(4.8)	(7.3)	(2.9)	(4.1)	(7.0)
Unearned fees applied against loan balance	(0.5)	—	(0.5)	(1.6)	(0.2)	(1.8)
Ending unearned income balance	$ 4.9	$ 8.3	$ 13.2	$ 5.6	$ 10.8	$ 16 4

(a) When a loan is paid off at an amount below our cost basis, we apply any fees received that have not been recognized as income against the outstanding loan amount to reduce the cost basis, which has the effect of reducing any realized loss.

Other Fees

In certain investment transactions, we perform investment banking and other advisory services. For services that are separately identifiable and external evidence exists to substantiate fair value, income is recognized as earned which is generally when the investment transaction closes.

Valuation of Investments

At September 30, 2004, approximately 78% of our total assets represented investments recorded at fair value. Value, as defined in Section 2(a)(41) of the Investment Company Act of 1940, is (i) the market price for those securities for which a market quotation is readily available and (ii) for all other securities and assets, fair value is as determined in good faith by the board of directors. Since there is typically no readily available market value for the investments in our portfolio, we value substantially all of our investments at fair value as determined in good faith by the board of directors pursuant to a valuation policy and a consistent valuation process. Because of the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments determined in good faith by the board of directors may differ significantly from the values that would have been used had a ready market existed for the investments, and the differences could be material.

There is no single standard for determining fair value in good faith. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment. Unlike banks, we are not permitted to provide a general reserve for anticipated loan losses. Instead, we must determine the fair value of each individual investment on a quarterly basis. We will record unrealized depreciation on investments when we believe that an investment has decreased in value, including where collection of a loan or realization of an equity security is doubtful. Conversely, we will record unrealized appreciation if we believe that the underlying portfolio company has appreciated in value and, therefore, our investment has also appreciated in value, where appropriate.

As a business development company, we invest primarily in illiquid securities including debt and equity securities of private companies. The structure of each debt and equity security is specifically negotiated to enable us to protect our investment and maximize our returns. We generally include many terms governing interest rate, repayment terms, prepayment penalties, financial covenants, operating covenants, ownership and corporate governance parameters, dilution parameters, liquidation preferences, voting rights, and put or call rights. In many cases, our loan agreements also allow for increases in the spread to the base index rate if the financial or operational performance of the customer deteriorates or shows negative variances from the customer's business plan and, in some cases, allow for decreases in the spread if financial or operational performance improves or exceeds the customer's plan. Our investments are generally subject to some restrictions on resale and generally have no established trading market. Because of the type of investments that we make and the nature of our business, our valuation process requires an analysis of various factors. Our fair value methodology includes the examination of, among other things, the underlying investment performance, financial condition and market changing events that impact valuation.

With respect to private debt and equity securities, each investment is valued using industry valuation benchmarks, and, where appropriate, the value is assigned a discount reflecting the illiquid nature of the investment and/or our minority, non-control position. When an external event such as a purchase transaction, public offering, or subsequent debt or equity sale occurs, the pricing indicated by the external event will be used to corroborate our private debt or equity valuation. Securities that are traded in the over-the-counter market or on a stock exchange generally will be valued at the prevailing bid price on the valuation date. However, restricted or thinly traded public securities may be valued at discounts from the public market value due to the restrictions on sale.

Stock-based Compensation

We account for stock-based compensation under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. For restricted common stock issued to employees for whom no return-based criteria apply, compensation expense, equal to the value of the shares at the later of the grant date or the date at which all return-based forfeiture provisions lapsed or were removed, is recorded over the term of the forfeiture provisions. See Note 5 to the Consolidated Financial Statements for further discussion of our employee stock plans.

Securitization Transactions

Periodically, we transfer pools of loans to special purpose entities (SPEs) for use in securitization transactions. These on-balance sheet securitization transactions comprise a significant source of our overall funding, with the total face amount of the outstanding loans and equity investments assumed by third parties equaling $518.7 million at September 30, 2004 and $441.8 million at December 31, 2003. On April 1, 2001, the Company adopted the requirements of SFAS No. 140, "*Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* ", which applies prospectively to all securitization transactions occurring after March 31, 2001. Adoption of SFAS No. 140 did not have a material impact on our operations or financial position. Transfers of loans have not met the requirements of SFAS No. 140 for sales treatment and are, therefore, treated as secured borrowings, with the transferred loans remaining in investments and the related liability recorded in borrowings.

Recent Development

On October 29, 2004, MCG portfolio company, Bridgecom Holdings, Inc., entered into a merger agreement with Broadview Networks Holdings, Inc. The merger is expected to close in the first quarter of 2005 and is subject to regulatory approvals, the consent to the merger by Broadview's lenders and other closing conditions. Given the conditions to closing, there can be no assurance as to the timing of close or that the transaction will close.

Risk Factors

Investing in our common stock involves a high degree of risk. You should consider carefully the risks described below and all other information contained in this quarterly report, including our financial statements and the related notes and the schedules and exhibits to this quarterly report.

Risks Related to Our Business and Financial Results

We have a limited operating history as a business development company and as a regulated investment company, which may impair your ability to assess our prospects.

Prior to our initial public offering in December 2001, we had not operated as a business development company under the Investment Company Act of 1940 or as a regulated investment company under Subchapter M of the Internal Revenue Code. As a result, we have limited operating results under these regulatory frameworks that can demonstrate to you either their effect on our business or our ability to manage our business under these frameworks. In addition, prior to our initial public offering, our management had no prior experience managing a business development company or regulated investment company. We cannot assure you that we will be able to operate successfully as a business development company and a regulated investment company.

Because there is generally no established market for which to value our investments, our board of directors' determination of the value of our investments may differ materially from the values that a ready market or third party would attribute to these investments.

Under the 1940 Act, we are required to carry our portfolio investments at market value or, if there is no readily available market value, at fair value as determined by our board. We are not permitted to maintain a general reserve for anticipated loan losses. Instead, we are required by the 1940 Act to specifically value each individual investment and to record any unrealized depreciation for any asset that we believe has decreased in value. Because there is typically no public market for the loans and equity securities of the companies in which we invest, our board will determine the fair value of these loans and equity securities on a quarterly basis pursuant to our valuation policy. These determinations of fair value necessarily will be somewhat subjective. Accordingly, these values may differ significantly from the values that would be determined by a third party or placed on the portfolio if there existed a market for our loans and equity securities.

We make loans to and invest in primarily small- and medium-sized privately owned companies, which may default on their loans, thereby reducing or eliminating the return on our investments.

Our portfolio primarily consists of loans to and securities issued by small- and medium-sized privately owned businesses. Compared to larger publicly owned firms, these companies may be more vulnerable to economic downturns, may have more limited access to capital and higher funding costs, may have a weaker financial position, and may need more capital to expand or compete. These businesses also may experience substantial variations in operating results. They may face intense competition, including from companies with greater financial, technical and marketing resources. Typically, they also depend for their success on the management talents and efforts of an individual or a small group of persons. The death, disability or resignation of any of their key employees could harm their financial condition. Furthermore, some of these companies do business in regulated industries and could be affected by changes in government regulation. Accordingly, these factors could impair their cash flow or result in other events, such as bankruptcy, which could limit their ability to repay their obligations to us, and may adversely affect the return on, or the recovery of, our investment in these businesses Deterioration in a borrower's financial condition and prospects may be accompanied by deterioration in any collateral for the loan.

Some of these companies may be unable to obtain financing from public capital markets or from traditional credit sources, such as commercial banks. Accordingly, advances made to these types of customers may entail a higher risk of loss than advances made to customers who are able to utilize traditional credit sources. These conditions may also make it difficult for us to obtain repayment of our loans.

Furthermore, there is generally no publicly available information about such companies and we must rely on the diligence of our employees to obtain information in connection with our investment decisions. If we are unable to uncover all material information about these companies, we may not make a fully informed investment decision and we may lose money on our investments.

If the industry sectors in which our portfolio is concentrated experience adverse economic or business conditions, our operating results may be negatively impacted.

Our customer base is primarily in the communications, information services, media and technology, including software and technology-enabled business services, industry sectors These customers can experience adverse business conditions or risks related to their industries.

- Many media companies rely on advertising, which tends to be cyclical and influenced by macro-economic factors, as their primary revenue stream. In addition, many media companies are subject to risks associated with the increasing cost of raw material commodities such as paper, printing and postage, and broadcasters are subject to the risks associated with a regulated environment. Within the last two years, we have been negatively affected by our customers in the magazine publishing sector, in particular those with substantial exposure to financial services, telecommunications and technology advertising. These advertising categories experienced steeper declines than the general advertising market.

- Communications companies often have high customer acquisition costs and require significant liquidity. As a result, these companies require significant infusions of capital and would be adversely affected by a disruption in their ability to raise capital. In addition, such companies are subject to the risks associated with a changing regulatory environment. Much of the current difficulty facing the industry is a function of overcapacity and speculation by investors related to ongoing deregulation and future demand related to the internet and emerging broadband applications.

- Information services businesses are subject to risks associated with their dependence on intellectual property assets. If their ability to access critical intellectual property rights is impaired, their businesses could be suddenly and adversely affected. Other risks for information services businesses include the possibility of innovations that render certain services obsolete.

- Providers of technology, including software and technology-enabled business services, may experience significant costs in keeping their products and services technologically up-to-date. Some also have high fixed costs and capital expenditure requirements that require significant access to capital.

Accordingly, if our customers suffer (as some customers currently are) due to these adverse business conditions or risks or due to economic slowdowns or downturns in these industry sectors, we will be more vulnerable to losses in our portfolio and our operating results may be negatively impacted. Furthermore, if demand for financing by existing and new customers in these industries declines, we may not be able to increase our lending and investment volume and our operating results will be adversely affected.

Economic downturns or recessions could impair our customers' ability to repay our loans, harm our operating results and reduce our volume of new loans.

Many of our customers may be susceptible to economic downturns or recessions and may be unable to repay our loans during these periods. Therefore, our non-performing assets are likely to increase and the value of our portfolio is likely to decrease during these periods. Adverse economic conditions also may decrease the value of collateral securing some of our loans and the value of our equity investments. Economic downturns or recessions could lead, to financial losses in our portfolio and a decrease in net income. Unfavorable economic conditions could also lead to a decrease in revenues and assets.

An economic downturn could disproportionately impact the industry sectors in which we concentrate causing us to be more vulnerable to losses in our portfolio and experience diminished demand for capital in these industry sectors and, consequently, our operating results may be negatively impacted.

At September 30, 2004 and December 31, 2003, there were $0.1 million and $4.2 million, respectively, of loans, or approximately 0.01% and 0.6%, respectively, of the investment portfolio, greater than 60 days past due At September 30, 2004, $12.0 million of loans, including all of the loans greater than 60 days past due, were on non-accrual status, which represented 1.5% of the investment portfolio. At December 31, 2003, $14.6 million of loans, including $0.1 million of the loans greater than 60 days past due, were on non-accrual status, which represented 2.1% of the investment portfolio. The non-accrual and past due loans at September 30, 2004 and December 31, 2003 primarily represented borrowers in the publishing, telecommunications and paging businesses. Portions of the trade publishing industry, which are dependent on financial, technology or telecommunications advertising, experienced sluggish advertising revenue. Certain companies in the telecommunications industry have suffered from competitive pressure from low cost and prepaid cellular calling plans. At September 30, 2004, of the $121.2 million of loans to our majority owned portfolio companies, $12.0 million were on non-accrual status. At December 31, 2003, of the $83.1 million of loans to our majority owned portfolio companies, $10.5 million were on non-accrual status At September 30, 2004, of the $36.6 million of loans to our controlled non-majority owned portfolio companies, none were on non-accrual status. At December 31, 2003, of the $18.6 million of loans to our controlled non-majority owned portfolio companies, $3.9 million were on non-accrual status As of September 30, 2004, of the $52.3 million of loans to other affiliates, none were on non-accrual status. As of December 31, 2003, of the $45 6 million of loans to other affiliates, $0.2 million were on non-accrual status.

Unfavorable economic conditions also could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us These events could prevent us from increasing our loan originations and investments and harm our operating results.

If we fail to qualify as a regulated investment company, we will have to pay corporate-level taxes on our income and our income available for distribution would be reduced.

We elected to be taxed for federal income tax purposes as a regulated investment company under Subchapter M of the Internal Revenue Code with the filing of our federal corporate income tax return for 2002, which election was effective as of January 1, 2002. If we can meet certain requirements, including source of income, asset diversification and distribution requirements, as well as if we continue to qualify as a business development company, we will qualify to be a regulated investment company and will not have to pay corporate-level taxes on any income we distribute to our stockholders as dividends, allowing us to substantially reduce or eliminate our corporate-level tax liability. Covenants and provisions in our credit facilities limit the ability of our subsidiaries and our securitization trusts to make distributions to us, which could affect our ability to make distributions to our stockholders and to maintain our status as a regulated investment company In addition, we may have difficulty meeting the requirement to make distributions to our stockholders because in certain cases we may recognize income before or without receiving cash representing such income. If we fail to qualify as a regulated investment company, we will have to pay corporate-level taxes on all of our income whether or not we distribute it, which would substantially reduce the amount of income available for distribution to our stockholders. Even if we qualify as a regulated investment company, we generally will be subject to a corporate-level income tax on the income we do not distribute. Moreover, if we do not distribute at least 98% of our income, we generally will be subject to a 4% excise tax.

Because we will distribute substantially all of our income to our stockholders, we will continue to need additional capital to finance our growth. If additional capital is unavailable or not available on favorable terms, our ability to grow will be impaired.

In order to satisfy the requirements applicable to a regulated investment company, we intend to distribute to our stockholders all of our income except for certain net capital gains. We expect to elect to make deemed distributions to our stockholders of the retained net capital gains. In addition, as a business development company, we generally will be required to meet a coverage ratio of total assets to total senior securities, which include all of our borrowings and any preferred stock we may issue in the future, of at least 200%. This requirement limits the amount that we may borrow. Because we will continue to need capital to grow our loan and investment portfolio, this limitation may prevent us from incurring debt and require us to raise additional equity at a time when it may be disadvantageous to do so. Additional financing may not be available on favorable terms, if at all, or may be restricted by the terms of our securitization facilities. If additional funds are not available to us, we could be forced to curtail or cease our new lending and investment activities, and our net asset value could decrease.

We have substantial indebtedness and servicing our indebtedness could reduce funds available to grow our business.

As of September 30, 2004, we had $446.4 million of outstanding borrowings under our securitization facilities and $25.0 million of outstanding borrowings under our Senior Secured Revolving Credit Facility. As a result, our current financial structure has a high proportion of debt and our debt service is substantial. As of September 30, 2004, the weighted average annual interest rate on all of our outstanding borrowings was 2.38%. In order for us to cover our annual interest payments on indebtedness, we must achieve annual returns on our September 30, 2004 total assets of at least 1.07%. Our ability to service our debt depends largely on our financial performance and will be subject to prevailing economic conditions and competitive pressures.

In addition, our subsidiaries have sold some of our loans to trusts that serve as the vehicles for our securitization facilities, and we do not hold legal title to these assets. However, we bear losses of principal and interest from defaults on these loans held by the trusts up to the amount of our retained interest in the trusts, which was approximately $160.2 million as of September 30, 2004.

Our securitization facilities impose financial and operating covenants that restrict our business activities, including limitations that could hinder our ability to finance additional loans and investments or to make the distributions required to maintain our status as a regulated investment company under Subchapter M of the Internal Revenue Code.

Borrowings, also known as leverage, magnify the potential for gain or loss on amounts invested and, therefore, increase the risks associated with investing in our securities. Leverage is generally considered a speculative investment technique. If the value of our consolidated assets increases, then leveraging would cause the net asset value attributable to our common stock to increase more than it otherwise would have had we not used leverage. Conversely, if the value of our consolidated assets decreases, leveraging would cause net asset value attributable to our common stock to decline more than it otherwise would have had we not used leverage. Similarly, any increase in our consolidated revenue in excess of consolidated interest expense on our borrowed funds would cause our net income to increase more than it would without the use of leverage. Any decrease in our consolidated revenue would cause net income to decline more than it would have had we not borrowed funds and could negatively affect our ability to make distributions on our common stock.

As a business development company, we generally are required to meet a coverage ratio of total assets to total borrowings and other senior securities, which include all of our borrowings and any preferred stock we may issue in the future, of at least 200%. If this ratio declines below 200%, we may not be able to incur additional debt and may need to sell a portion of our investments to repay some debt when it is disadvantageous to do so, and we may not be able to make distributions. At September 30, 2004, this ratio was approximately 221%.

In addition, because substantially all of our assets and liabilities are priced using various short-term rate indices, including one-month to six-month LIBOR, commercial paper rates and the prime rate, the timing of changes in market interest rates or in the relationship between interest rate indices could affect the interest rates earned on interest-earning assets differently than the interest rates paid on interest-bearing liabilities, which could result in a decrease in net income.

If we are not able to refinance our debt or able to do so on favorable terms, we would not be able to operate our business in the ordinary course.

Our 2001-1 Term Securitization Facility is scheduled to terminate on February 20, 2013 or sooner upon repayment of our borrowings, our 2004-1 Term Securitization Facility is scheduled to terminate on July 20, 2016 or sooner upon repayment of our borrowings, and our Senior Secured Revolving Credit Facility is scheduled to expire on September 30, 2005.

We cannot assure you that we will be able to extend the terms of these facilities or obtain sufficient funds to repay any amounts outstanding under these facilities before they expire or terminate either from a replacement facility or alternative debt or equity financing If we are unable to repay amounts outstanding under these facilities and are declared in default or are unable to refinance these facilities, we would not be able to operate our business in the regular course Even if we are able to refinance our debt, we may not be able to do so on favorable terms.

You may not receive distributions.

We intend to make distributions on a quarterly basis to our stockholders. We may not be able to achieve operating results that will allow us to make distributions at a specific level or to increase the amount of these distributions from time to time. In addition, due to the asset coverage test applicable to us as a business development company, we may be limited in our ability to make distributions. See "Regulation as a Business Development Company" in the accompanying prospectus. Also, restrictions and provisions in our securitization facilities limit our ability to make distributions. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax consequences, including possible loss of our status as a regulated investment company. We cannot assure you that you will receive any distributions or distributions at a particular level.

We may have difficulty paying our required distributions if we recognize income before or without receiving cash representing such income.

In accordance with generally accepted accounting principles and tax regulations, we include in income certain amounts that we have not yet received in cash, such as contracted payment-in-kind interest, which represents contractual interest added to the loan balance and due at the end of the loan term. The increases in loan balances as a result of contracted payment-in-kind arrangements are included in income in advance of receiving cash payment, and are separately identified on our consolidated statements of cash flows. Since we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our investment company taxable income to maintain our status as a regulated investment company. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies".

If we fail to manage our growth, our financial results could be adversely affected.

We have expanded our operations rapidly since purchasing our business from First Union National Bank in 1998. Our growth has placed and could continue to place significant strain on our management systems and resources. We must continue to refine and expand our marketing capabilities, our management of the investment process, our access to financing resources and our technology. As we grow, we must continue to hire, train, supervise and manage new employees We may not develop sufficient lending and administrative personnel and management and operating systems to manage our expansion effectively. If we are unable to manage our growth, our operations could be adversely affected and our financial results could be adversely affected.

If we need to sell any of our investments, we may not be able to do so at a favorable price and, as a result, we may suffer losses.

Our investments are usually subject to contractual or legal restrictions on resale or are otherwise illiquid because there is usually no established trading market for such investments. The illiquidity of most of our investments may make it difficult for us to dispose of them at a favorable price, and, as a result, we may suffer losses. In addition, if we were forced to immediately liquidate some or all of the investments in our portfolio, the proceeds of such liquidation could be significantly less than the current value of such investments. We may be required to liquidate some or all of our portfolio to meet our debt service obligations or to maintain our qualification as a business development company and as a regulated investment company if we do not satisfy one or more of the applicable criteria under the respective regulatory frameworks.

Our business depends on our key personnel.

Our future success depends to a significant extent on the continued services of Bryan J. Mitchell, our Chief Executive Officer, Steven F. Tunney, our President and Chief Operating Officer, B. Hagen Saville, one of our Executive Vice Presidents, and Robert J. Merrick, our Chief Credit Officer, as well as other key personnel. Mr. Mitchell was diagnosed in May 1999 with adenocarcinoma, a form of colon cancer, for which he was treated through surgery and a series of post-operative treatments that ended in December 1999. Mr. Mitchell's illness is in remission and has not significantly impaired his ability to perform his duties. The loss of any of these key employees would likely have a significant detrimental effect on our business. In addition, if any two of Mr. Mitchell, Mr. Saville, Mr. Tunney or Mr. Merrick cease to be actively involved in our management, the lender under one of our securitization facilities could, absent a waiver or cure, replace us as the servicer of the loans and declare a default. In addition, if any two of Mr. Mitchell, Mr. Tunney or Mr. Saville cease to be an executive officer of MCG actively in the management of MCG, the lender of our $25 million senior secured credit facility could, absent a waiver or cure, declare a default.

Fluctuations in interest rates could adversely affect our income.

A significant increase in market interest rates could harm our ability to attract new customers and originate new loans and investments, our non-performing assets could increase and the value of our portfolio could decrease because our floating-rate loan customers may be unable to meet higher payment obligations. Conversely, a significant decrease in interest rates would reduce our net income, all other things being equal. A decrease in interest rates may reduce net income despite the increased demand for our capital that the decrease in interest rates may produce Approximately 90% of the loans in our portfolio, based on amounts outstanding at cost as of September 30, 2004, were at variable rates determined on the basis of a benchmark LIBOR or prime rate and approximately 10% were at fixed rates. From October 1, 2003 to September 30, 2004, three-month LIBOR has increased from 1.15% to 2.02%.

Regulations governing our operation as a business development company will affect our ability to, and the way in which we, raise additional capital.

We have issued debt securities and may issue debt securities and/or borrow money from banks or other financial institutions, which we refer to collectively as "senior securities," up to the maximum amount permitted by the 1940 Act Under the provisions of the 1940 Act, we are permitted, as a business development company, to issue senior securities only in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after each issuance of senior securities. If the value of our assets declines, we may be unable to satisfy this test. If that happens, we may be required to sell a portion of our investments and, depending on the nature of our leverage, repay a portion of our indebtedness at a time when such sales may be disadvantageous.

We are not generally able to issue and sell our common stock at a price below net asset value per share. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the current net asset value of the common stock if our board of directors determines that such sale is in the best interests of MCG Capital and its stockholders, and our stockholders approve such sale. In any such case, the price at which our securities are to be issued and sold may not be less than a price which, in the determination of our board of directors, closely approximates the market value of such securities (less any distributing commission or discount).

Any change in regulation of our business could negatively affect the profitability of our operations.

Changes in the laws, regulations or interpretations of the laws and regulations that govern business development companies, regulated investment companies or non-depository commercial lenders could significantly affect our operations and our cost of doing business. We are subject to federal, state and local laws and regulations and are subject to judicial and administrative decisions that affect our operations. If these laws, regulations or decisions change, or if we expand our business into jurisdictions that have adopted more stringent requirements than those in which we currently conduct business, we may have to incur significant expenses in order to comply or we might have to restrict our operations.

Our ability to invest in private companies may be limited in certain circumstances.

If we are to maintain our status as a business development company, we must not acquire any assets other than "qualifying assets" unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are qualifying assets. If we acquire debt or equity securities from an issuer that has outstanding marginable securities at the time we make an investment, these acquired assets generally cannot be treated as qualifying assets. This result is dictated by the definition of "eligible portfolio company" under the 1940 Act, which in part focuses on whether a company has outstanding marginable securities.

Amendments promulgated in 1998 by the Board of Governors of the Federal Reserve System expanded the definition of a marginable security under the Federal Reserve's margin rules to include any non-equity security. Thus, any debt securities issued by any entity are marginable securities under the Federal Reserve's current margin rules. As a result, the staff of the SEC has raised the question as to whether a private company that has outstanding debt securities would qualify under the relevant portion of the "eligible portfolio company" criteria. The SEC has recently issued proposed rules to include any company that does not have a class of securities listed on a national securities exchange or association in the definition of "eligible portfolio company."

Until the question raised by the staff of the SEC pertaining to the Federal Reserve's 1998 change to its margin rules has been addressed by final legislative, administrative or judicial action, we intend to treat as qualifying assets only those debt and equity securities that are issued by a private company that has no marginable securities outstanding at the time we purchase such securities or that otherwise qualifies as an "eligible portfolio company" under the 1940 Act.

Item 3.Quantitative and Qualitative Disclosures about Market Risk

Interest rate sensitivity refers to the change in earnings that may result from the changes in the level of interest rates. Our net interest income is affected by changes in various interest rates, including LIBOR, prime rates and commercial paper rates. Over 85% of our loan portfolio bears interest at a spread to LIBOR, with the remainder bearing interest at a fixed rate or at a spread to a prime rate. Approximately 52% of our loan portfolio has a LIBOR floor, at various levels Our interest rates on our borrowings are based on LIBOR and commercial paper rates, with the majority based on LIBOR. At September 30, 2004, the rate spread to LIBOR of our accruing loans and yielding equity investments was 10.0%.

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We regularly measure exposure to interest rate risk We have interest rate risk exposure mainly from the portion of the commercial loan portfolio funded using stockholders' equity. Our board of directors assesses interest rate risk and we manage our interest rate exposure on an ongoing basis. The following table shows a comparison of the interest rate base for our interest bearing cash, outstanding commercial loans and our outstanding borrowings at September 30, 2004 and December 31, 2003:

(dollars in millions)	September 30, 2004		December 31, 2003	
	InterestBearing Cash and CommercialLoans	Borrowings	InterestBearing Cash and CommercialLoans	Borrowings
Repurchase Agreement Rate	$ 218.7	$ —	$ 93.0	$ —
Prime Rate	30.4	—	1.3	—
30-Day LIBOR	48.5	—	20.9	—
60-Day LIBOR	14.3	—	7.4	—
90-Day LIBOR	507.5	471.4	481.6	173.1
180-Day LIBOR	35.6	—	—	—
Commercial Paper Rate	—	—	—	131.0
Fixed Rate	72.7	—	94.4	—
Total	$ 927.7	$ 471.4	$ 698.6	$ 304.1

Based on our September 30, 2004 balance sheet, the following table shows the impact of base rate changes in interest rates assuming no changes in our investment and borrowing structure. The impact of an additional 100 basis point increase is different from the first 100 basis point increase due to the imposition of LIBOR floors.

(dollars in millions)

Basis Point Change	Interest Income	Interest Expense	Net Income
(100)	$ (4.8)	$ (4.7)	$ (0.1)
100	$ 7.2	$ 4.7	$ 2.5
200	$ 15 8	$ 9.4	$ 6 4
300	$ 24 4	$ 14.1	$ 10.3

Currently, we do not engage in hedging activities because we have determined that the cost of hedging the risks associated with interest rate changes outweighs the risk reduction benefit We monitor this strategy on an ongoing basis.

Item 4.Controls and Procedures

As of the end of the period covered by this report, MCG carried out an evaluation, under the supervision and with the participation of MCG's management, including MCG's Chief Executive Officer, President and Chief Operating Officer, Chief Financial Officer and Chief Accounting Officer, of the effectiveness of the design and operation of MCG's disclosure controls and procedures (as defined in Rule 13a-15 of the Securities Exchange Act of 1934). Based on that evaluation, the Chief Executive Officer, the President and Chief Operating Officer, the Chief Financial Officer and Chief Accounting Officer have concluded that MCG's current disclosure controls and procedures are effective in timely alerting them of material information relating to MCG that is required to be disclosed by MCG in the reports it files or submits under the Securities Exchange Act of 1934.

(There have been no changes in MCG's internal control over financial reporting that occurred during the quarter ended September 30, 2004 that have materially affected, or are reasonably likely to materially affect, MCG's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1.Legal Proceedings

On January 29, 2003, a purported securities class action lawsuit was filed in the United States District Court for the Eastern District of Virginia against us, certain of our officers and the underwriters of our initial public offering. The complaint alleged that the defendants made certain misstatements in violation of Sections 11, 12(a) (2) and 15 of the Securities Act of 1933 and Section 10(b), Rule 10b-5 and Section 20(a) of the Securities Exchange Act of 1934. Specifically, the complaint asserted that members of the plaintiff class purchased our common stock at purportedly inflated prices during the period from November 28, 2001 to November 1, 2002 as a result of certain misstatements regarding the academic degree of our chief executive officer. The complaint sought unspecified compensatory and other damages, along with costs and expenses On June 16, 2003, a consolidated amended class action complaint was filed in the proceedings captioned In re MCG Capital Corporation Securities Litigation, 1:03cv0114-A. The consolidated amended complaint named only us and certain of our officers and directors as defendants, and alleged violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 We filed a motion to dismiss the consolidated amended class action complaint. On September 12, 2003, the United States District Court for the Eastern District of Virginia dismissed the lawsuit in its entirety. The plaintiffs filed a notice of appeal to seek review of the district court decision by the United States Court of Appeals for the Fourth Circuit, and both parties have now filed briefs. The appeal is pending.

We are also a party to certain legal proceedings incidental to the normal course of our business including the enforcement of our rights under contracts with our portfolio companies. While the outcome of these legal proceedings cannot at this time be predicted with certainty, we do not expect that these proceedings will have a material effect upon our financial condition or results of operations.

Item 2.Unregistered Sales of Equity Securities and Use of Proceeds

During the nine months ended September 30, 2004, MCG issued a total of 4,270 shares of common stock under its dividend reinvestment plan pursuant to an exemption from the registration requirements of the Securities Act of 1933. The aggregate offering proceeds for the shares of common stock sold under the dividend reinvestment plan were approximately $72 thousand. The proceeds were used for general corporate purposes

Item 3.Defaults Upon Senior Securities

Not Applicable.

Item 4.Submission of Matters to a Vote of Security Holders

Not Applicable.

Item 5.Other Information

Not Applicable.

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Item 6.Exhibits

Listed below are the exhibits which are filed as part of this report (according to the number assigned to them in Item 601 of Regulation S-K):

Exhibit Number	Description of Document
10.66*	Sale and Servicing Agreement by and among MCG Commercial Loan Trust 2004-1, MCG Finance IV, LLC, MCG Capital Corporation and Wells Fargo Bank, National Association, dated as of September 30, 2004.
10.67*	Indenture between MCG Commercial Loan Trust 2004-1 and Wells Fargo Bank, National Association, dated as of September 30, 2004.
31.1*	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
31.2*	Certification of President and Chief Operating Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
31.3*	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
31.4*	Certification of Chief Accounting Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.
32.1*	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U. S. C. 1350).
32.2*	Certification of President and Chief Operating Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U. S. C. 1350).
32.3*	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U. S. C. 1350).
32.4*	Certification of Chief Accounting Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).

* Submitted herewith.

SIGNATURES

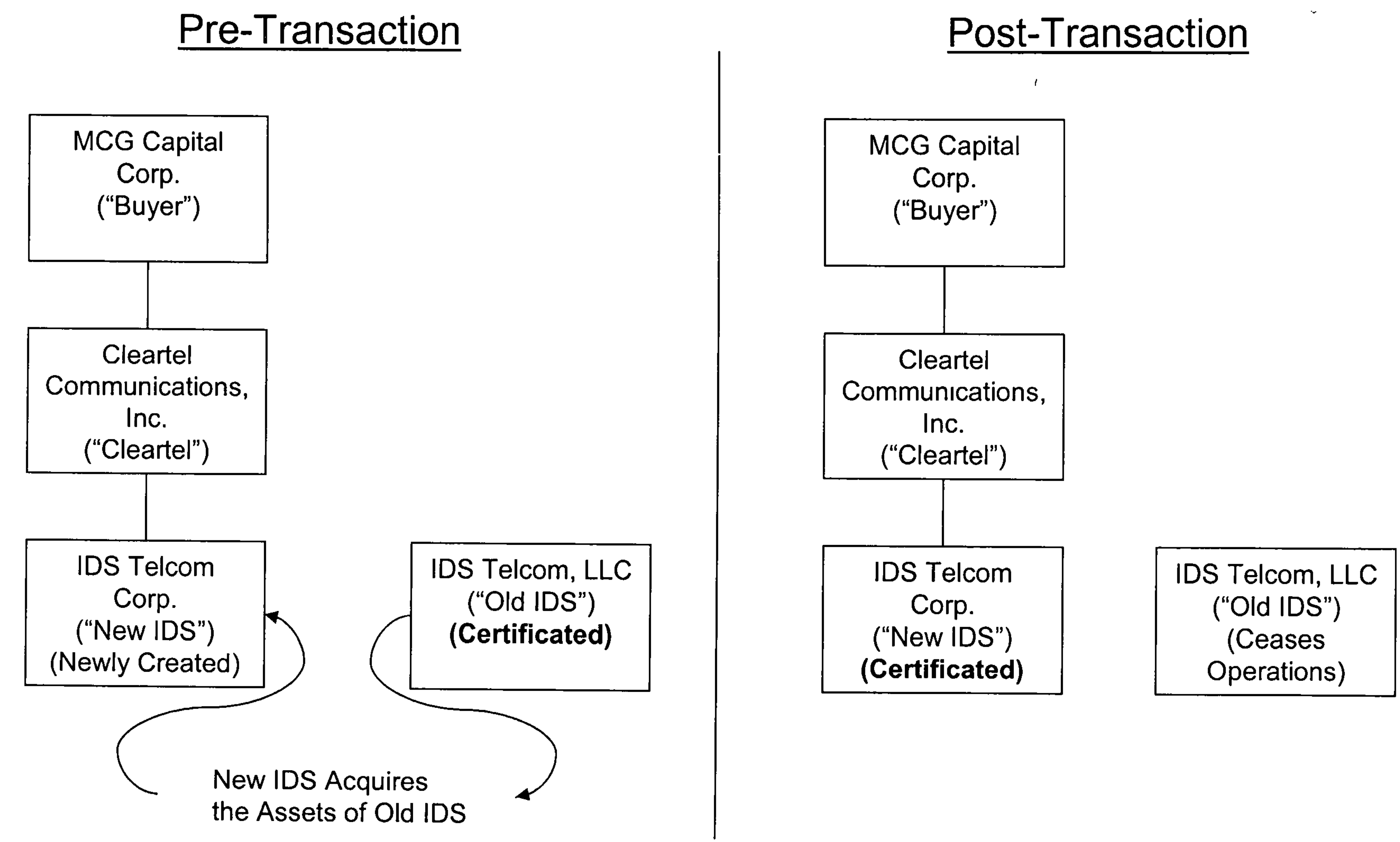
Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on November 4, 2004.

	MCG CAPITAL CORPORATION
By:	/s/BRYAN J. MITCHELL
	Bryan J. Mitchell
	Chief Executive Officer
By:	/s/STEVEN F. TUNNEY
	Steven F. Tunney
	President and Chief Operating Officer
By:	/s/MICHAEL R. MCDONNELL
	Michael R. McDonnell
	Chief Financial Officer
By:	/s/JOHN C. WELLONS
	John C. Wellons
	Chief Accounting Officer

EXHIBIT C

Illustrative Chart

Illustrative Chart



<u>EXHIBIT D</u>

New IDS Corporate Documents

In order to comply with certain name use rules, New IDS is currently registered with the Tennessee Secretary of State as operating under the fictitious name of "IDS Telcom Corp. of Delaware." Following the proposed transaction, however, IDS Telcom, LLC will cease operating and New IDS will operate under the name "IDS Telcom Corp." not "IDS Telcom Corp. of Delaware." Once available, documents demonstrating that change in formal corporate name will be filed with the Commission upon request.

Delaware

The First State

I, HARRIET SMITH WINDSOR, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY "IDS TELCOM CORP." IS DULY INCORPORATED UNDER THE LAWS OF THE STATE OF DELAWARE AND IS IN GOOD STANDING AND HAS A LEGAL CORPORATE EXISTENCE SO FAR AS THE RECORDS OF THIS OFFICE SHOW, AS OF THE FIFTH DAY OF JANUARY, A.D. 2005.

AND I DO HEREBY FURTHER CERTIFY THAT THE FRANCHISE TAXES HAVE NOT BEEN ASSESSED TO DATE.

AND I DO HEREBY FURTHER CERTIFY THAT THE SAID "IDS TELCOM CORP." WAS INCORPORATED ON THE FOURTH DAY OF JANUARY, A.D. 2005.

Harriet Smith Windsor

Harriet Smith Windsor, Secretary of State

3907301 8300

050008162

AUTHENTICATION: 3596975

DATE: 01-05-05

Delaware

The First State

I, HARRIET SMITH WINDSOR, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF INCORPORATION OF "IDS TELCOM CORP.", FILED IN THIS OFFICE ON THE FOURTH DAY OF JANUARY, A.D. 2005, AT 5:38 O'CLOCK P.M.

A FILED COPY OF THIS CERTIFICATE HAS BEEN FORWARDED TO THE NEW CASTLE COUNTY RECORDER OF DEEDS.

Harriet Smith Windsor

Harriet Smith Windsor, Secretary of State

3907301 8100

050006555

AUTHENTICATION: 3595916

DATE: 01-04-05

State of Delaware
Secretary of State
Division of Corporations
Delivered 05:45 PM 01/04/2005
FILED 05:38 PM 01/04/2005
SRV 050006555 - 3907301 FILE

CERTIFICATE OF INCORPORATION

OF

IDS TELCOM CORP.

Pursuant to § 102 of the General Corporation Law of the State of Delaware

The undersigned, in order to form a corporation pursuant to Section 102 of the General Corporation Law of Delaware, does hereby certify:

FIRST: The name of the Corporation is IDS Telcom Corp. (the "Corporation").

SECOND: The address of the Corporation's registered office in the State of Delaware is 2711 Centerville Road, Suite 400 in the City of Wilmington, County of New Castle, Delaware 19808. The name of its registered agent at such address is Corporation Service Company.

THIRD: The purpose of the Corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware.

FOURTH: The total number of shares of all classes of capital stock which the Corporation shall have the authority to issue is 1,000 shares of which:

500 shares, par value $0.01 per share, shall be shares of common stock (the "Common Stock"); and

500 shares, par value $0.01 per share, shall be shares of preferred stock (the "Preferred Stock").

A. Common Stock.

(1) Dividends. The holders of shares of Common Stock shall be entitled to receive, when and if declared by the Board of Directors, out of the assets of the

Corporation which are by law available therefor, dividends payable either in cash, in property, or in shares of Common Stock.

(2) Voting Rights. At every annual or special meeting of stockholders of the Corporation, every holder of Common Stock shall be entitled to one vote, in person or by proxy, for each share of Common Stock standing in his name on the books of the Corporation.

(3) Liquidation, Dissolution, or Winding Up. In the event of any voluntary or involuntary liquidation, dissolution, or winding up of the affairs of the Corporation, after payment or provision for payment of the debts and other liabilities of the Corporation, if any, the holders of all outstanding shares of Common Stock shall be entitled to share ratably in the remaining net assets of the Corporation.

B. Preferred Stock. The Board of Directors is authorized, subject to limitations prescribed by law, to provide by resolution or resolutions for the issuance of shares of Preferred Stock in one or more series, to establish the number of shares to be included in each such series, and to fix the voting powers (if any), designations, powers, preferences, and relative, participating optional or other rights, if any, of the shares of each such series, and any qualifications, limitations or restrictions thereof. Irrespective of the provisions of Section 242(b)(2) of the DGCL, the number of authorized shares of Preferred Stock may be increased or decreased (but not below the number of shares thereof then outstanding) by the affirmative vote of the holders of a majority in voting power of the stock of the Corporation entitled to vote, without the separate vote of the holders of the Preferred Stock as a class.

FIFTH: The name and mailing address of the Incorporator is as follows: Melanie J. Bosman, 523 McColley Street, Milford, DE 19963.

SIXTH: The Board of Directors is expressly authorized to adopt, amend, or repeal the Bylaws of the Corporation.

SEVENTH: Elections of directors need not be by written ballot unless the by-laws of the Corporation shall otherwise provide.

EIGHTH: A director of the Corporation shall not be personally liable to the Corporation or its stockholders for monetary damages for breach of fiduciary duty as a director; provided, however, that the foregoing shall not eliminate or limit the liability of a director (i) for any breach of the director's duty of loyalty to the Corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the General Corporation Law of Delaware, or (iv) for any transaction from which the director derived an improper personal benefit. If the General Corporation Law of Delaware is hereafter amended to permit further elimination or limitation of the personal liability of directors, then the liability of a director of the Corporation shall be eliminated or limited to the fullest extent permitted by the General Corporation Law of Delaware as so amended. Any repeal or modification of this Article EIGHTH by the stockholders of the Corporation or otherwise shall not adversely affect any right or protection of a director of the Corporation existing at the time of such repeal or modification.

NINTH: Melanie J. Bosman, 523 McColley Street, Milford, Delaware is appointed as sole director of the Corporation until his successor is appointed in accordance with the by-laws of the Corporation or the Delaware General Corporation Law.

TENTH: The Corporation reserves the right to amend, alter, change, or repeal any provision contained in this Certificate of Incorporation, in the manner now or hereafter prescribed by statute, and all rights conferred upon stockholders herein are granted subject to this reservation.

IN WITNESS WHEREOF, I have hereunto set my hand this 4th day of January, 2005 and I affirm that the foregoing certificate is my act and deed and that the facts stated therein are true.

/s/ Melanie J. Bosman

Melanie J. Bosman, Incorporator

ISSUANCE DATE: 01/31/2005
REQUEST NUMBER: 05031112A

Secretary of State
Division of Business Services
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, Tennessee 37243

CHARTER/QUALIFICATION DATE: 01/28/2005
STATUS: ACTIVE
CORPORATE EXPIRATION DATE: PERPETUAL
CONTROL NUMBER: 0486235
JURISDICTION: DELAWARE

TO:
CFS
8161 HIGHWAY 100
#172
NASHVILLE, TN 37221

REQUESTED BY:
CFS
8161 HIGHWAY 100
#172
NASHVILLE, TN 37221

I, RILEY C DARNELL, SECRETARY OF STATE OF THE STATE OF TENNESSEE DO HEREBY CERTIFY THAT

"IDS TELCOM CORP."

WAS INCORPORATED OR QUALIFIED TO DO BUSINESS IN THE STATE OF TENNESSEE ON THE ABOVE DATE, AND THAT THE ATTACHED DOCUMENT(S) WAS/WERE FILED IN OFFICE ON THE DATE(S) AS BELOW INDICATED:

REFERENCE NUMBER	DATE FILED	FILING TYPE	FILING ACTION NAM DUR STK PRN OFC AGT INC MAL FYC
5343-2891	01/28/2005	QUAL-PROFIT	
5343-2895	01/28/2005	ASSUMED-ADD	

FOR: REQUEST FOR COPIES

ON DATE: 01/31/05

FEES

FROM:
CFS
8161 HIGHWAY 100
#172
NASHVILLE, TN 37221-0000

RECEIVED: $200.00 $0.00
TOTAL PAYMENT RECEIVED: $200.00
RECEIPT NUMBER: 00003640058
ACCOUNT NUMBER: 00101230

THE GREAT SEAL OF THE STATE OF TENNESSEE XVI AGRICULTURE COMMERCE 1796

Riley C Darnell

RILEY C DARNELL
SECRETARY OF STATE

SS-4458

State of Tennessee

Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, TN 37243

APPLICATION FOR CERTIFICATE OF AUTHORITY (FOR PROFIT)

For Office Use Only

FILED

2005 JAN 28 PM 1:12

SECRETARY OF STATE

Pursuant to the provisions of Section 48-25-103 of the Tennessee Business Corporation Act, the undersigned corporation hereby applies for a certificate of authority to transact business in the State of Tennessee, and for that purpose sets forth:

1 The name of the corporation is IDS Telcom Corp

*If different, the name under which the certificate of authority is to be obtained is IDS Telcom Corp of Delaware

[NOTES: The Secretary of State of the State of Tennessee may not issue a certificate of authority to a foreign corporation for profit if its name does not comply with the requirements of Section 48-14-101 of the Tennessee Business Corporation Act *If obtaining a certificate of authority under a different corporate name, an application for registration of an assumed corporate name must be filed pursuant to Section 48-14-101(d) with an additional $20 00 fee]

2. The state or country under whose law it is incorporated is Delaware

3. The date of its incorporation is January 4, 2005 (must be month, day, and year), and the period of duration, if other than perpetual, is ______

4. The complete street address (including zip code) of its principal office is

Street	City	State/Country	Zip Code
2855 South Congress Avenue	Delray Beach	Florida	33445

5. The complete street address (including the county and the zip code) of its registered office in Tennessee and the name of its registered agent is

Street	City	State/Country	Zip Code
2908 Poston Avenue	Nashville	TN	37203

Registered Agent Corporation Service Company

6. The names and complete business addresses (including zip code) of its current officers are: (Attach separate sheet if necessary)
See attached Rider

7. The names and complete business addresses (including zip code) of its current board of directors are: (Attach separate sheet if necessary) See attached Rider

8 If the corporation commenced doing business in Tennessee prior to the approval of this application, the date of commencement (month, day and year) n/a.

9. The corporation is a corporation for profit.

10. If the document is not to be effective upon filing by the Secretary of State, the delayed effective date/time is ______, ______(date), ______(time).

[NOTE: A delayed effective date shall not be later than the 90th day after the date this document is filed by the Secretary of State]

[NOTE: This application must be accompanied by a certificate of existence (or a document of similar import) duly authenticated by the Secretary of State or other official having custody of corporate records in the state or country under whose law it is incorporated The certificate shall not bear a date of more than two (2) months prior to the date the application is filed in this state]

January 19, 2005
Signature Date

IDS Telcom Corp
Name of Corporation

ASSISTANT SECRETARY
Signer's Capacity

Scott Kellogg
Signature

SCOTT KELLOGG
Name (typed or printed)

IDS TELCOM CORP. OFFICER AND DIRECTOR INFORMATION RIDER

OFFICERS:

Officer Name	Office	Address
Kenneth Baritz	Chief Executive Officer & President	2855 South Congress Avenue Delray Beach, FL 33445
Jim Doherty	Chief Operating Officer	2855 South Congress Avenue Delray Beach, FL 33445
Don Zyck	Vice President-Finance	2855 South Congress Avenue Delray Beach, FL 33445
Terie Hannay	Vice President-Fiscal Operations	2855 South Congress Avenue Delray Beach, FL 33445
Michelle Baker	Treasurer	2855 South Congress Avenue Delray Beach, FL 33445
Michael Burman	Secretary	2855 South Congress Avenue Delray Beach, FL 33445
Scott Kellogg	Assistant Secretary	2855 South Congress Avenue Delray Beach, FL 33445

DIRECTOR:

Kenneth Baritz	2855 South Congress Avenue Delray Beach, FL 33445

Delaware

The First State

I, HARRIET SMITH WINDSOR, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY "IDS TELCOM CORP." IS DULY INCORPORATED UNDER THE LAWS OF THE STATE OF DELAWARE AND IS IN GOOD STANDING AND HAS A LEGAL CORPORATE EXISTENCE SO FAR AS THE RECORDS OF THIS OFFICE SHOW, AS OF THE TWENTY-FOURTH DAY OF JANUARY, A.D. 2005.

AND I DO HEREBY FURTHER CERTIFY THAT THE SAID "IDS TELCOM CORP." WAS INCORPORATED ON THE FOURTH DAY OF JANUARY, A.D. 2005.

AND I DO HEREBY FURTHER CERTIFY THAT THE FRANCHISE TAXES HAVE NOT BEEN ASSESSED TO DATE.

Harriet Smith Windsor

Harriet Smith Windsor, Secretary of State

3907301 8300

050057626

AUTHENTICATION: 3636634

DATE: 01-24-05

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5348 0305

State of Tennessee

Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R Snodgrass Tower
Nashville, TN 37243

APPLICATION FOR REGISTRATION OF ASSUMED CORPORATE NAME

For Office Use Only

RECEIVED

2005 JAN 28 PM 1:12

RILEY DARNELL
SECRETARY OF STATE

Pursuant to the provisions of Section 48-14-101(d) of the Tennessee Business Corporation Act or Section 48-54-101(d) of the Tennessee Nonprofit Corporation Act, the undersigned corporation hereby submits this application:

1. The true name of the corporation is IDS Telcom Corp.

2 The state or country of incorporation is Delaware.

3. The corporation intends to transact business in Tennessee under an assumed corporate name.

4. The assumed corporate name the corporation proposes to use is
IDS Telcom Corp. of Delaware.

[NOTE: The assumed corporate name must meet the requirements of Section 48-14-101 of the Tennessee Business Corporation Act or Section 48-54-101 of the Tennessee Nonprofit Corporation Act.]

January 19, 2005
Signature Date

IDS Telcom Corp.
Name of Corporation

ASSISTANT SECRETARY
Signer's Capacity

Scott Kellogg
Signature

SCOTT KELLOGG
Name (typed or printed)

SS-4402 (Rev 4/01) Filing Fee $20 RDA1720

Secretary of State
Division of Business Services
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, Tennessee 37243

DATE: 01/31/05
REQUEST NUMBER: 5343-2895
TELEPHONE CONTACT: (615) 741-2286
FILE DATE/TIME: 01/28/05 1312
EFFECTIVE DATE/TIME:
CONTROL NUMBER: 0486235

TO:
CSC
1201 HAYS STREET

TALLAHASSEE, FL 32301

RE:
IDS TELCOM CORP. OF DELAWARE
APPLICATION FOR REGISTRATION OF ASSUMED CORPORATE NAME

THIS WILL ACKNOWLEDGE THE FILING OF THE ATTACHED ASSUMED NAME REGISTRATION FOR A FIVE YEAR PERIOD BEGINNING WITH AN EFFECTIVE DATE AS INDICATED ABOVE.

THE CORPORATION MAY RENEW THE RIGHT TO USE THIS NAME WITHIN TWO (2) MONTHS PRECEDING THE EXPIRATION OF SUCH RIGHT, FOR A PERIOD OF FIVE (5) YEARS, BY FILING AN APPLICATION WITH THE SECRETARY OF STATE.

WHEN CORRESPONDING WITH THIS OFFICE OR SUBMITTING DOCUMENTS FOR FILING, PLEASE REFER TO THE CORPORATION CONTROL NUMBER GIVEN ABOVE.

FOR: APPLICATION FOR REGISTRATION OF ASSUMED CORPORATE NAME

ON DATE: 01/31/05

FROM:
CSC (1201 HAYS STREET)
1201 HAYS STREET

TALLAHASSEE, FL 32301-0000

	FEES	
RECEIVED:	$20.00	$0.00
TOTAL PAYMENT RECEIVED:		$20.00

RECEIPT NUMBER: 00003639689
ACCOUNT NUMBER: 00254020

Riley C Darnell

RILEY C DARNELL
SECRETARY OF STATE

SS-4458

5

5343-2895

State of Tennessee Department of State Corporate Filings 312 Eighth Avenue North 6th Floor, William R Snodgrass Tower Nashville, TN 37243	**APPLICATION FOR REGISTRATION OF ASSUMED CORPORATE NAME**	*For Office Use Only* 2005 JAN 28 PM 1:12 SECRETARY OF STATE

Pursuant to the provisions of Section 48-14-101(d) of the Tennessee Business Corporation Act or Section 48-54-101(d) of the Tennessee Nonprofit Corporation Act, the undersigned corporation hereby submits this application:

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2. The state or country of incorporation is Delaware.

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IDS Telcom Corp. of Delaware.

[NOTE: The assumed corporate name must meet the requirements of Section 48-14-101 of the Tennessee Business Corporation Act or Section 48-54-101 of the Tennessee Nonprofit Corporation Act]

January 19, 2005
Signature Date

IDS Telcom Corp
Name of Corporation

ASSISTANT SECRETARY
Signer's Capacity

Signature

SCOTT KELLOGG
Name (typed or printed)

EXHIBIT E

Customer Notice Letter

DRAFT
FORM OF NOTICE

Dear Valued IDS Customers,

We are pleased to announce an asset purchase agreement between IDS Telcom, LLC and IDS Telcom Corp., a Cleartel Communications company. This agreement will become effective and IDS Telcom Corp. will become your service provider on or about March 31, 2005

During the past twelve months we've worked hard to create new product offerings and streamline provisioning and customer service processes The end result is a stronger communications company to serve you better

There are several assurances we want to make to you, our highly valued customer. First, especially in today's marketplace, IDS Telcom Corp , a Cleartel Communications company is committed to meeting the highest possible customer service standards.

Second, we can assure you that the hundreds of fine employees at IDS Telcom Corp are committed to providing our customers with the best in telecommunications quality and services Additionally and perhaps most importantly, Cleartel has the experience and resources to ensure that IDS Telcom Corp meets your telecommunications needs. Cleartel Communications is a national Competitive Local Exchange Carrier, operating in over twenty nine states. Our mission is providing exceptional value through superior customer support and advanced services.

It's also important for you to know.

- The services you have paid for will not be impacted as a result of this agreement
- Your existing rates and charges will not be changed as a result of this transaction.
- You will still pay for/renew your services in the same way you do today

We recognize that you have the right to choose you telephone service provider If you do choose another provider you may incur installation or carrier change charges If you stay with Old IDS, however, you will not incur any such charges for the transfer to IDS Telcom Corp Further, you will not need to take any action for the transfer to IDS Telcom Corp. to occur (Additionally we will maintain any preferred carrier freeze you may have).

If you have any questions about this notice or problems with your current service, please call IDS at 1-888-707-6500 To ensure a seamless transition of service, please note that IDS Telcom Corp. intends to keep that same number after the transition

We appreciate your business and your commitment to IDS during this transitional time. The future looks bright as we move forward with new bundled local/long distance products, Internet services including web hosting and broadband internet solutions to residential and small business customers

Sincerely,

IDS Telcom Corp. IDS Telcom, LLC

VERIFICATION

STATE OF ILLINOIS	)
COOK COUNTY	)

I, Scott Kellogg, declare under penalty of perjury that I am Associate General Counsel and Assistant Secretary of IDS Telcom Corp., a Petitioner in the subject proceeding; that I am authorized to make this verification on the Petitioner's behalf; that I have read the foregoing Petition and know the contents thereof; and that the same are true of my own knowledge, except as to the matters which are therein stated on information or belief, and as to those matters I believe them to be true.

Scott Kellogg
Associate General Counsel and
Assistant Secretary
IDS Telcom Corp.

Subscribed and sworn to before me

this 27th day of JANUARY, 2005.

Angeline C Grano
Notary Public

My Commission Expires: 5-7-2007

"OFFICIAL SEAL"
ANGELINE C GRANO
Notary Public, State of Illinois
My Commission Expires 05/07/2007

VERIFICATION

STATE OF FLORIDA)

MIAMI-DADE COUNTY)

I, Joseph C. Millstone, declare under penalty of perjury that I am Chief Executive Officer of IDS Telcom, LLC, a Party in the subject proceeding; that I am authorized to make this verification on the Party's behalf; that I have read the foregoing filing and know the contents thereof; and that the same are true of my own knowledge, except as to the matters which are therein stated on information or belief, and as to those matters I believe them to be true.

Joseph C. Millstone
Chief Executive Officer
IDS Telcom, LLC

Subscribed and sworn to before me
this 1st day of February, 2005.

Notary Public

My Commission Expires:

OFFICIAL NOTARY SEAL
ANGEL M LEIRO
NOTARY PUBLIC STATE OF FLORIDA
COMMISSION NO. CC800603
MY COMMISSION EXP. JAN. 6,2007

Tennessee